

**UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF MISSOURI
EASTERN DIVISION**

DOUGLAS R. ROE, on behalf of himself)
and Arch Coal, Inc. Employee Thrift Plan,)
and/or alternatively on behalf of a class)
consisting of similarly situated)
participants of the Plan,)

Plaintiff,)

Case no. 4:15-cv-00910

v.)

ARCH COAL, INC.; THE FINANCE)
COMMITTEE OF THE BOARD OF)
DIRECTORS OF ARCH COAL, INC.;)
THEODORE D. SANDS; JOHN W. EAVES;)
J. THOMAS JONES; GEORGE C. MORRIS III;)
PAUL A. LANG; JAMES A. SABALA;)
STEVEN F. LEER; ROBERT G. POTTER;)
BRIAN J. JENNINGS; A. MICHAEL PERRY;)
PETER I WOLD; THE INTERNAL)
RETIREMENT COMMITTEE OF ARCH COAL;)
ALLEN R. KELLEY; JOHN ZIEGLER, JR.;)
JOHN DOES 1-10, and MERCER FIDUCIARY)
TRUST COMPANY,)

Defendants.)

JURY TRIAL DEMANDED

CLASS ACTION COMPLAINT

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Plaintiff Douglas R. Roe (“Plaintiff”), on behalf of the Arch Coal, Inc. Employee Thrift Plan (the “Plan”),¹ himself, and, to the extent necessary, a class of similarly situated participants of the Plan (the “Participants”), for his Complaint, states as follows:

INTRODUCTION

1. Plaintiff, a Participant in the Plan during time periods relevant to the Complaint, bring this action under Section 502(a) of the Employee Retirement Income Security Act (“ERISA”), 29 U.S.C. § 1132(a), for Plan-wide relief based upon the Plan’s purchases and holdings of shares of common stock of Arch Coal, Inc. (“Arch” or the “Company”) common stock (“Arch Stock”) or units of any Arch Coal Common Stock Fund (the “Fund”)² from January 1, 2012 to the present, inclusive (the “Relevant Period”).³ This action is brought derivatively, for Plan-wide relief for breaches of fiduciary duty, pursuant to § 502(a)(2) of ERISA, 29 U.S.C. § 1132(a)(2). As more fully set forth below, Defendants breached their ERISA fiduciary duties, including those fiduciary duties set forth in Section 404, 29 U.S.C. § 1104, and Department of Labor Regulations, including 29 C.F.R. § 2550.

2. In the alternative, Plaintiff brings this action as a class action pursuant to Fed. R. Civ. P. 23(a) and Fed. R. Civ. P. 23(b)(1) and/or (b)(3) of the Federal Rules of Civil Procedure, on behalf of the following class of persons similarly situated (the “Class”):

All Participants for whose individual accounts the Plan held shares of Arch Stock or Fund units during the Relevant Period.

¹ An earlier iteration of the Plan’s governing document (the “Plan Document”) was filed as Exhibit 99.1 to an August 4, 1997 Form S-8 filed with the Securities and Exchange Commission (the “SEC”).

² Fund units and Arch common stock in the Plan are used interchangeably herein.

³ Plaintiff reserves his right to seek to modify the Relevant Period if discovery reveals a more appropriate period. *See, e.g., Lively v. Dynegy*, No. 05-CV-00063, 2007 WL 685861, at *6 (S.D. Ill. Mar. 2, 2007) (“the proper termination date of the proposed class period is the date when Dynegy stock ceased to be, as Plaintiff alleges, an imprudent investment for the Plan”).

3. The Plan is a legal entity that can sue and be sued. ERISA § 502(d)(1), 29 U.S.C. § 1132(d)(1). However, in a breach of fiduciary duty action such as this, the Plan is not a party. Rather, pursuant to ERISA § 409 the relief requested in this action is for the benefit of the Plan.

4. 401(k) plans confer tax benefits on participating employees to incentivize saving for retirement. An employee participating in a 401(k) plan may have the option of purchasing the common stock of his or her employer, often the sponsor of the plan, for part of his or her retirement investment portfolio. Arch Stock was one of the investment alternatives of the Plan throughout the Relevant Period.

5. Plaintiff allege that Defendants, as “fiduciaries” of the Plan pursuant to ERISA § 3(21)(A), 29 U.S.C. § 1002(21)(A), breached duties owed to the Plan, to Plaintiff, and the Participants by, *inter alia*, retaining Arch Stock as an investment option in the Plan when a reasonable fiduciary using the “care, skill, prudence, and diligence... that a prudent man acting in a like capacity and familiar with such matters would use” would have done otherwise. *See* ERISA § 404(a)(1), 29 U.S.C. § 1104(a)(1).

6. Specifically, Plaintiff alleges in Count I that Defendants, each having certain responsibilities regarding the management and investment of the Plan’s assets, breached their fiduciary duties to the Plan, to them, and the proposed Class by: (a) continuing to offer Arch Stock as a Plan investment option when it was imprudent to do so; and (b) maintaining the Plan’s pre-existing significant investment in Arch Stock when it was no longer a prudent investment for the Plan. These actions/inactions run directly counter (a) to the express purpose of ERISA pension plans, which are designed to help provide funds for participants’ retirement (*see* ERISA § 2, 29 U.S.C. § 1001 (“CONGRESSIONAL FINDINGS AND DECLARATION OF POLICY”)) and (b) the purpose of the Plan (*i.e.*, to help Participants save for retirement).

7. Plaintiff's Count II alleges that certain Defendants breached their fiduciary duties by failing to adequately monitor other persons to whom management/administration of the Plan's assets was delegated, despite the fact that such Defendants knew or should have known that such other fiduciaries were imprudently allowing the Plan to continue offering Arch Stock as an investment option, and investing the Plan's assets in Arch Stock when it was imprudent to do so.

8. Plaintiff's Count III alleges that Mercer Fiduciary Trust Company ("Mercer") breached its fiduciary duties by blindly following the directions of the Plan's named fiduciaries, in violation of ERISA, when it was clearly imprudent to do so. Mercer continued to allow the Plan to hold and acquire Arch Stock when it was clear, based upon publicly available information, that Arch Stock was an objectively imprudent retirement savings vehicle.

9. The thrust of Plaintiff's allegations is Defendants allowed imprudent investment of the Plan's assets in Arch Stock throughout the Relevant Period when they knew or should have known that such investment was imprudent as a retirement vehicle because of the sea-change in the coal industry and because the business prospects of Arch were dismal. Indeed, by the start of 2012, there was tremendous upheaval in the worldwide and domestic coal markets, including a large portion of the coal markets ceding to cheap natural gas. It was unclear whether the changes would be cyclical or secular (although many experts increasingly predicted the later), and if and when they might reverse. *Dow Jones Business News* reported in an article on January 17, 2012, that "U.S. coal producers had seen their stocks plummet recently as the companies have battled against rising costs, increased environmental oversight and stiffer competition from cleaner-burning and sometimes cheaper natural gas. Coal is expected to cede more market share to natural gas, *in what analysts say could be a permanent shift.*" (emphasis added).⁴

⁴ Bolded and italicized text herein is emphasized, unless otherwise noted.

10. As a consequence of the foregoing (as described in significantly more detail below), and under the circumstances as they existed in the market at the time, no reasonably prudent ERISA fiduciary would have concluded that Arch Stock was a sufficiently safe investment for Participants' retirement savings, and no reasonably prudent ERISA fiduciary would have maintained the Plan's investment in Arch Stock as a result of the tremendous risk of what became essentially a pure coal play: a gamble that coal would turn-around before Arch's liquidity dried up, and would rise above the price where it previously had been trading.

11. Defendants knew or should have known that significant investment of Participants' retirement savings in Arch Stock would be unduly risky and was unreasonably likely to result in substantial losses to the Plan and, consequently, to the Participants.

12. Defendants recognized or should have recognized the severity of the crisis at Arch during the Relevant Period but took no steps to protect the Plan as conditions worsened, or alternatively waited until it was far too late for such changes to make any meaningful difference. Indeed, it appears based upon a Plan rollover contribution form⁵ that the Arch Coal Common Stock Fund is still accepting contributions. A fiduciary who simply ignores changed circumstances that have increased the risk of loss to the trust's beneficiaries is imprudent.

13. ERISA requires fiduciaries to employ appropriate methods to investigate the merits of all plan investments and to engage in a reasoned decision-making process, consistent with that of a prudent person acting in a like capacity. ERISA's duty of prudence requires fiduciaries to monitor the prudence of their investment decisions to ensure that the investments remain in the best interest of a plan's participants.

⁵ mlit.mercerhrs.com/ec/RLC/ParticipantServlet?requestID=displayPDFFile&itemID=/IFS/ARCHCOAL650595009.pdf

14. Prudent investment management demands, *inter alia*, that Defendants not merely rely upon the fact that Arch Stock's price remained above \$0 and that it had not filed for bankruptcy in determining whether investing in Company Stock was appropriate for the Plan. ERISA required Defendants to scrutinize the risk of continued Plan investment in Arch Stock—based upon, *inter alia*, the public information upon which the stock price was based and the risk inherent therein—to protect the Participants' retirement savings.

15. Aside from its price, which has plummeted drastically and steadily during the Relevant Period, trading for less than a dollar at times during 2015, Arch Stock was and is an imprudent investment for the Plan, as shown herein.

16. Even if it may have been a reasonable investment for some investors, ERISA requires fiduciaries to avoid taking excessive risk with retirement assets. After all, "the duties of prudence and loyalty embodied in [ERISA § 404(a)(2)] have been characterized as the 'highest known to law.'" *See, e.g., Shannahan v. Dynegy, Inc.*, No. 06-cv-0160, 2006 WL 3227319, at *4 (S.D. Tex. Nov. 6, 2006) (quoting *Sommers Drug Stores Co. Employee Profit Sharing Trust v. Corrigan*, 793 F.2d 1456, 1468 (5th Cir. 1986)).

17. Evaluating the prudence of an investment decision requires a totality-of-the-circumstances inquiry taking into account the character and aim of the particular plan and decision at issue and the circumstances prevailing at the time. The Plan, which was meant to be a vehicle for retirement savings, required less risky and objectively prudent investments.

18. The Plan was intended to assist Participants in accumulating benefits for retirement. Trust Law, from which ERISA is derived, cautions that "[t]he duty of care requires the trustee to exercise reasonable effort and diligence in planning the administration of the trust, in making and implementing administrative decisions, and in monitoring the trust situation, *with*

due attention to the trust's objectives and the interests of the beneficiaries.” Restatement (Third) of Trusts § 77, Comment b (emphasis added).

19. The Participants had every right under ERISA to expect—and did expect—that the Plan’s fiduciaries would act in their interest and protect them from unduly risky investments, whether in Company Stock or any other asset.

20. Moreover, at least some of the Defendants, given the facts described herein, failed to provide the Participants information necessary to make informed decisions regarding Arch Stock. Plaintiff does not allege that Arch Stock was artificially inflated because of the withholding of such information, but rather that Defendants had a duty under ERISA to disclose that information, cause the Plan to cease purchasing Arch Stock, cause the Plan to divest of unduly risky investments in Arch Stock, and/or take other steps as necessary and appropriate to avoid the Plan’s massive losses.

21. By apparently conducting no investigation, analysis, or review with respect to whether it was prudent to continue investment in Arch Stock in the Plan, Defendants acted procedurally imprudently. Had Defendants conducted a prudent evaluation the appropriateness of Arch Stock for the Plan during the Relevant Period, and taken protective action as described below, Participants would not have suffered such devastating losses to their retirement savings.

22. This action is brought on behalf of the Plan and seeks recovery of the losses to the Plan for which Defendants are liable because of their actions or lack thereof. *See* ERISA § § 409 and 502, 29 U.S.C. § § 1109 and 1132. Given the totality of circumstances prevailing during the Relevant Period, no prudent fiduciary would have made the same decision to retain the clearly imprudent Arch Stock as a Plan investment or to allow Participants to continue investing their retirement savings in Arch Stock.

JURISDICTION AND VENUE

23. ***Subject Matter Jurisdiction.*** This Court has subject matter jurisdiction over this action pursuant to 28 U.S.C. § 1331 and ERISA § 502(e)(1), 29 U.S.C. § 1132(e)(1).

24. ***Personal Jurisdiction.*** This Court has personal jurisdiction over all Defendants because they are all residents of the United States and ERISA provides for nation-wide service of process pursuant to ERISA § 502(e)(2), 29 U.S.C. § 1132(e)(2).

25. ***Venue.*** Venue is proper in this district pursuant to ERISA § 502(e)(2), 29 U.S.C. § 1132(e)(2), because the Plan is administered in this district, some or all of the fiduciary breaches for which relief is sought occurred in this district, and one or more Defendants reside or may be found in this district.

PARTIES

Plaintiff

26. Plaintiff Douglas R. Roe is a former Arch employee. He is a “participant” in the Plan, within the meaning of ERISA § 3(7), 29 U.S.C. § 1102(7), and held shares of Arch Stock in his retirement investment portfolio during the Relevant Period.

Defendants

The Company

27. Defendant Arch is a diversified coal company engaged in coal production, marketing and supply of cleaner-burning, low-sulfur thermal and metallurgical coal to power generators and steel manufacturers over five continents. The Company’s business segments include the Powder River Basin (PRB), with operations in Wyoming; the Appalachia (APP), with operations in West Virginia, Kentucky, Maryland and Virginia. Its domestic reserve base consists of more than 5 billion tons of metallurgical and thermal coal reserves and represents 14% of America’s coal supply from active mining complexes in Wyoming, Colorado, Illinois,

West Virginia, Kentucky, Virginia and Maryland. The Company is incorporated in Delaware and maintains its principal place of business at City Place One Ste 300, St. Louis, Mo 63141.

28. Arch was the Plan's sponsor and was a fiduciary of the Plan during the whole of the Relevant Period. Arch breached its fiduciary and co-fiduciary duties as described below.

29. Arch, acting through its Board of Directors' Finance Committee, appointed the persons who managed and administered the Plan. Arch is legally responsible for the malfeasance of its Directors and appointed persons alleged herein. Instead of delegating fiduciary duties for the Plan to outside service providers, Arch chose to internalize the Plan's fiduciary functions and, upon information and belief, appointed its employees as Plan fiduciaries.

Finance Committee Defendants

30. Defendant Finance Committee of the Arch Board of Directors (the "Finance Committee") was tasked by its charter⁶

4. To review and evaluate annually the Company's status and performance in the employee benefit plan area. This review shall include, as a minimum:

- ◆ Actuarial valuations
- ◆ Investment policies
- ◆ Individual investment manager's performance
- ◆ Internal Retirement Committee performance

31. Defendants Theodore D. Sands,⁷ John W. Eaves, J. Thomas Jones, George C. Morris III, Paul A. Lang, James A. Sabala, Steven F. Leer, Robert G. Potter, Brian J. Jennings, A. Michael Perry, and Peter I Wold (collectively the "Finance Committee Members" and with

⁶ Available at investor.archcoal.com/phoenix.zhtml?c=107109&p=irolgovCommittee&Committee=8761

⁷ Defendant Sands was the Chairman of the Finance Committee during the Relevant Period.

the “Finance Committee”, the “Finance Committee Defendants” or the “Monitoring Defendants”), by virtue of their membership on the Finance Committee, were fiduciaries of the Plan, within the meaning of ERISA Section 3(21)(A), 29 U.S.C. § 1002(21)(A), during part or all of the Relevant Period because they exercised discretionary authority or control over Plan management and/or authority or control over management or disposition of Plan assets.

Retirement Committee Defendants

32. Defendant Retirement Committee was, as stated in the Plan’s June 26, 2014 Form 11-K Annual Report Pursuant to Section 15(d) of the Securities Exchange Act of 1934 (the “2014 11-K”), “established [by the Company] to oversee the activities of the Plan and [the Company] has appointed the Vice President - Human Resources as the Plan Administrator.”⁸

33. Defendant Allen R. Kelley signed the 2014 11-K as “Plan Administrator.” Upon information and belief, Defendant Kelley was a fiduciary of the Plan, within the meaning of ERISA Section 3(21)(A), 29 U.S.C. § 1002(21)(A), because he exercised discretionary authority or control over Plan management and/or authority or control over management or disposition of Plan assets.

34. Defendant John Ziegler, Jr. signed the Plan’s 2013 Form 11-K on June 26, 2013 and the Plan’s 2012 Form 11-K on June 27, 2012. Upon information and belief, Defendant Ziegler was a fiduciary of the Plan, within the meaning of ERISA Section 3(21)(A), 29 U.S.C. § 1002(21)(A), because he exercised discretionary authority or control over Plan management and/or authority or control over management or disposition of Plan assets.

⁸ The members of the Retirement Committee are not presently known to Plaintiff. Plaintiff believes that after a reasonable opportunity for discovery to obtain committee charters, meeting minutes, and other relevant information, will provide additional evidentiary support for the allegations set forth herein, including the identification of other Plan fiduciaries.

Additional “John Doe Defendants”

35. To the extent that there are additional Arch officers, directors, and employees who were fiduciaries of the Plan during the Relevant Period, including members of the Retirement Committee, the identities of whom are currently unknown to Plaintiff, Plaintiff reserves the right, once their identities are ascertained, to seek leave to join them to the instant action. Thus, without limitation, unknown “John Doe” Defendants 1-10 include other individuals, including, but not limited to, Company officers, directors, and employees, who were fiduciaries of the Plan within the meaning of ERISA Section 3(21)(A), 29 U.S.C. § 1002(21)(A) during the Relevant Period. The John Doe Defendants, together with the Retirement Committee and Defendants Kelley and Ziegler are referred to herein as the “Retirement Committee Defendants.”

Trustee Defendant

36. Defendant Mercer Fiduciary Trust Company maintains an office at 701 Market St. Suite 1100, St. Louis, MO 63101. Mercer was the Plan’s trustee and held Plan assets in trust. Mercer was a fiduciary of the Plan because it exercised discretionary authority or control over Plan management and/or authority or control over management or disposition of Plan assets.

THE PLAN

37. The 2014 11-K sets out the following Description of the Plan:

The Arch Coal, Inc. Employee Thrift Plan (the Plan) was established by Arch Coal, Inc. (the Company) for the benefit of the eligible employees of the Company, its subsidiaries and controlled affiliates.

The following description of the Plan provides only general information. Participants should refer to the Plan Document for a more complete description of the Plan’s provisions.

Certain provisions of the Plan, as described below, do not apply to or have been modified for certain subsidiaries and affiliates of the Company.

General

The Plan is a defined contribution plan that covers substantially all salaried employees, nonunion hourly employees, and certain union employees where specified by applicable collective bargaining agreements of the Company, its subsidiaries, and any controlled affiliates that elect to participate in the Plan. It is subject to the provisions of the Employee Retirement Income Security Act of 1974 (ERISA).

Contributions

Participants may elect to defer between 1% and 50% of compensation. Highly compensated employees may contribute up to 16% of compensation. Participants who have attained age 50 before the end of the Plan year are eligible to make catch-up contributions. Participants may also contribute amounts representing distributions from other qualified defined benefit or defined contribution plans (rollover). The Company is required to make matching contributions to all participants equal to 100% of the participant salary deferral contributions up to the first 6% of eligible compensation, with the exception of participants who are hourly eligible employees of Mountain Laurel, who instead, receive a fixed 8% employer contribution.

The Plan includes an automatic enrollment provision for all eligible employees. The automatic enrollment provides for default salary deferral contributions of 6% of eligible compensation, which will be invested in a target retirement fund. The participant has the option to make changes to the salary deferral percentage and investment allocation at any time.

Participant Accounts

Each participant's account is credited with the participant's salary deferral and rollover contributions; the Company's matching contribution, and Company discretionary contributions, if applicable, and an allocation of Plan earnings. The allocation of earnings is determined by the earnings of the participant's investment selection based on each participant's account balance, as defined in the Plan Document. In addition, each participant's account is charged for applicable Plan expenses. The benefit to which a participant is entitled is the benefit that can be provided from the participant's vested account.

* * *

Investment Options

Upon enrollment in the Plan, a participant may direct contributions in a number of investment options offered by the Plan.

Administrative Expense

Generally, all expenses related to the administration of the Plan are paid from Plan assets. Fees related to the administration of notes receivable from participants and investment advisory services are charged directly to the participant's account and are included in administrative expenses.

38. The 2014 11-K further states that

The Company has established a Retirement Committee to oversee the activities of the Plan and has appointed the Vice President - Human Resources as the Plan Administrator. Mercer Fiduciary Trust Company and Mercer HR Services (collectively, Mercer) is the Trustee and Recordkeeper for the Plan, respectively.

39. Despite the problems alleged herein, the Fund acquired millions of shares of Arch common stock during the Relevant Period and lost tens of millions of dollars of Participant's retirement savings as a result of Defendants' breaches of their fiduciary duties. As shown by the Forms 11-K filed on behalf of the Plan, the Plan's holdings during the Relevant Period were:

	<u>Holdings</u>	<u>Close</u>	<u>Approx. Shares Held</u>	<u>\$ Lost In Calendar Year</u>
Year-end 2011	\$27,824,221.00	\$14.51	1,917,589	(29,830,923)
Year-end 2012	\$23,324,416.00	\$7.32	3,186,396	(13,615,918)
Year-end 2013	\$17,580,458.00	\$4.45	3,950,665	(9,541,677)
Year-end 2014	Available late June 2015			
Total:				(\$52,988,518.00)

Plan Fiduciaries Are Bound By ERISA's Strict Standards

40. Despite the Plan's substantial investment in Arch Stock, Defendants failed to protect the Plan and its Participants from the decline in value of Company Stock resulting from the extreme risk inherent in Company Stock detailed below. Defendants not only continued to have the Plan hold shares of Arch Stock, they compounded the problem and the Plan's losses by having the Plan purchase additional shares during the Relevant Period.

41. Fiduciaries of retirement plans such as the Plan are bound by core ERISA fiduciary duties, including the duties to act loyally, prudently, and for the exclusive purpose of providing benefits to plan participants. This is true regardless of the structure of the plan, including whether the plan is styled as an ESOP.

42. Accordingly, if the fiduciaries of a plan know, or if an adequate investigation would reveal, that company stock is no longer a prudent investment for that plan, then the fiduciaries must disregard any plan direction to maintain investments in such stock and protect the plan by investing the plan assets in other, suitable, prudent investments.

ALTERNATIVE CLASS ACTION ALLEGATIONS

43. As noted above, Plaintiff brings this action derivatively pursuant to § 502(a)(2) and (3) of the Employee Retirement Income Security Act (“ERISA”), 29 U.S.C. § 1132(a)(2) and (3). Alternatively, Plaintiff brings this action as a class action pursuant to Rules 23(a), (b)(1)(B) and/or (b)(3) of the Federal Rules of Civil Procedure, on behalf of the Class defined in paragraph 2.

44. The members of the Class are so numerous that joinder of all members is impracticable. While the exact number of Class members is unknown to Plaintiff at this time and can only be ascertained through appropriate discovery, Plaintiff believes that there are, at minimum, thousands of members of the Class. The Plan’s 2013 Form 5500 tax return lists 7,863 Participants as of December 31, 2013.

45. Common questions of law and fact exist as to all members of the Class, which predominate over any questions affecting solely individual members of the Class. Among the questions of law and fact common to all members of the Class are:

- (a) Whether Defendants were Plan fiduciaries;
- (b) Whether Defendants breached their fiduciary duties to the Plan, Plaintiff

and/or the members of the Class;

(c) Whether the Plan and the Participants were injured by such breaches; and

(d) Whether the Plan and the Participants are entitled to damages and/or injunctive relief.

46. Plaintiff's claims are typical of the claims of the other members of the Class, as Plaintiff and all other members of the Class sustained injury arising out of Defendants' wrongful conduct in breaching their fiduciary duties and violating ERISA as complained of herein.

47. Plaintiff will fairly and adequately represent and protect the interests of the Class. Plaintiff has retained able counsel with extensive experience in class action ERISA litigation. The interests of Plaintiff are coincident with and not antagonistic to the interests of the other members of the Class.

48. Prosecution of separate actions by Participants would create a risk of inconsistent adjudications with respect to individual members of the Class which could establish incompatible standards of conduct for Defendants, or adjudications with respect to individual members of the Class would, as a practical matter, be dispositive of the interests of the other members or substantially impair or impede their ability to protect their interests.

DEFENDANTS' FIDUCIARY STATUS

49. ERISA requires every plan to provide for one or more named fiduciaries who will have "authority to control and manage the operation and administration of the plan." ERISA § 402(a)(1), 29 U.S.C. § 1102(a)(1).

50. ERISA treats as fiduciaries not only persons explicitly named as fiduciaries under § 402(a)(1), 29 U.S.C. § 1102(a)(1), but also any other persons who in fact perform fiduciary functions (*e.g.*, *de facto* or functional fiduciaries). Thus, a person acts as a fiduciary to the extent "(i) he exercises any discretionary authority or discretionary control respecting management of

such plan or exercises any authority or control respecting management or disposition of its assets, (ii) he renders investment advice for a fee or other compensation, direct or indirect, with respect to any moneys or other property of such plan, or has any authority or responsibility to do so, or (iii) he has any discretionary authority or discretionary responsibility in the administration of such plan.” ERISA § 3(21)(A)(i), 29 U.S.C. § 1002(21)(A)(i).

51. During the Relevant Period, upon information and belief, each of the Defendants was a fiduciary—*i.e.* either a named fiduciary or a *de facto* fiduciary—with respect to the Plan and owed fiduciary duties to the Plan and its Participants under ERISA. As fiduciaries, Defendants were required by ERISA § 404(a)(1), 29 U.S.C. § 1104(a)(1), to manage and administer the Plan, and the Plan’s investments solely in the interest of a plan’s participants and with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims.

52. Plaintiff does not allege that each Defendant was a fiduciary with respect to all aspects of the Plan’s management and administration. Rather, as set forth below, Defendants were fiduciaries to the extent of the specific fiduciary discretion and authority assigned to or exercised by each of them, and, as further set forth below, the claims against each Defendant are based on such specific discretion and authority.

53. Instead of delegating all fiduciary responsibility for the Plan to external service providers, the Company chose to assign the appointment and removal of fiduciaries, such as the members of the Retirement Committee, to itself through its Finance Committee.

54. ERISA permits fiduciary functions to be delegated to insiders without an automatic violation of the rules against prohibited transactions, ERISA § 408(c)(3), 29 U.S.C.

§ 1108(c)(3), but insider fiduciaries, like external fiduciaries, must act solely in the interest of participants, not in the interest of the plan sponsors.

55. During the Relevant Period, all of Defendants acted as fiduciaries of the Plan pursuant to ERISA § 3(21)(A), 29 U.S.C. § 1002(21)(A), and the law interpreting that section.

The Finance Committee Defendants' Fiduciary Status

56. As noted above, the Finance Committee Defendants were responsible for appointing the Retirement Committee Defendants.

57. Moreover, because the Finance Committee Defendants had the authority to appoint the members of the Retirement Committee, and the Retirement Committee was responsible for administering the Plan, the Finance Committee Defendants had the duty to monitor the activities of the Retirement Committee.

58. As a result, the Finance Committee Defendants had the ultimate responsibility for appointing, monitoring and, if necessary, removing Arch officers/employees delegated duties with respect to the administration and management of the Plan and management of the Plan's assets, including members of the Retirement Committee.

The Retirement Committee Defendants' Fiduciary Status

59. The Retirement Committee Defendants served as the Plan's "named fiduciary."

60. At all times relevant to this Complaint, the Retirement Committee Defendants were fiduciaries of the Plan as defined by ERISA Section 3(21)(A), 29 U.S.C. § 1002(21)(A), because they exercised discretionary authority or control respecting management of the Plan or exercised discretionary authority or control respecting management or disposition of Plan assets and had discretionary authority or responsibility in the administration of the Plan.

61. Each Defendant is liable for the breaches of fiduciary duty of the other Defendants under ERISA Section 405, 29 U.S.C. § 1105.

The Trustee's Fiduciary Status

62. A directed trustee cannot blindly follow directions of other fiduciaries; it is an ERISA fiduciary and has a duty to “supervise” and “investigate” the directions it receives from a plan’s named fiduciary when it has “some reason to know” that the directions may conflict with ERISA or a plan’s terms. Pursuant to ERISA Section 403(a)(1), 29 U.S.C. § 1103(a)(1), a directed trustee may only follow “proper directions” that are “not contrary to ERISA.”

63. Because Mercer, during the Relevant Period, knew or should have known that Arch was unduly risky for retirement savings, it had a fiduciary duty to protect the Participants and the Plan from the continued imprudent investment in Arch Stock.

Additional Fiduciary Aspects of Defendants' Actions/Inactions

64. ERISA plan fiduciaries have a duty of loyalty to a plan and its participants which includes the duty to speak truthfully to plans and their participants when communicating with them. “[L]ying is inconsistent with the duty of loyalty owed by all fiduciaries and codified in section 404(a)(1) of ERISA.” *Varity Corp. v. Howe*, 516 U.S. 489, 506 (1996).

65. Moreover, an ERISA fiduciary’s duty of loyalty requires the fiduciary to correct the inaccurate, incomplete or misleading information so that plan participants will not be injured.

66. During the Relevant Period, upon information and belief, Defendants made direct and indirect communications to Participants, including statements regarding investments in Company Stock. These communications included, but were not limited to, SEC filings, annual reports, press releases, and Plan documents (including SPDs and/or prospectuses regarding Plan/participant holdings of Company Stock), which included and/or reiterated these statements.

67. Plaintiff does not herein allege that Arch’s SEC filings were fiduciary communications. However, as the Solicitor General and the Solicitor of Labor asserted in their Brief for the United States as *Amicus Curiae* in *Fifth Third Bancorp v. Dudenhoeffer*, No. 12-751

(the “*Fifth Third Amicus*”),⁹ the incorporation of SEC filings into a SPD can be actionable under ERISA. *Id.* at 20-23; *accord Rinehart v. Akers*, 722 F.3d 137, 152 (2d Cir. 2013) (overruled in part on other grounds) (persons “act[] as ERISA fiduciaries when they incorporate[] [an employer’s] SEC filings into the SPD distributed to plan-participants.”) Thus, Defendants acted as fiduciaries to the extent they communicated with Participants about all Plan investments.

68. In their communications to the Participants, given the facts described herein, Defendants failed to provide the Participants information necessary to make informed decisions regarding Arch Stock. Plaintiff does not allege that Arch Stock was artificially inflated because of the withholding of such information, but rather that Defendants had a duty under ERISA to disclose that information, cause the Plan to cease purchasing and holding Arch Stock, and/or take other steps as necessary and appropriate to avoid massive Plan losses.

69. Further, Defendants, as the Plan’s fiduciaries, knew or should have known certain basic facts about the characteristics and behavior of the Participants, well-recognized in the 401(k) literature and the trade press concerning investment in company stock, including that:

- a. Employees tend to interpret a match in company stock as an endorsement of the company and its stock;
- b. Out of loyalty, employees tend to invest in company stock;
- c. Employees tend to over-extrapolate from recent returns, expecting high returns to continue or increase going forward;
- d. Employees tend not to change their investment option allocations in the plan once made;

⁹ Available at: [www.dol.gov/sol/media/briefs/dudenhoffer\(A\)-11-01-2013.pdf](http://www.dol.gov/sol/media/briefs/dudenhoffer(A)-11-01-2013.pdf)

e. No qualified retirement professional would advise rank and file employees to invest more than a modest amount of retirement savings in company stock, and many retirement professionals would advise employees to avoid investment in company stock entirely;

f. Lower income employees tend to invest more heavily in company stock than more affluent workers, though they are at greater risk; and

g. Even for risk-tolerant investors, the risks inherent to company stock are not commensurate with its rewards.

70. Even though Defendants knew or should have known these facts, and even though Defendants knew of the substantial investment of the Plan's assets in Company Stock, they still took no action to protect the Plan's assets from their imprudent investment in Arch Stock.

71. What is important is not whether Arch's executives and officers, including the fiduciaries of the Plan, were optimistic about the Company's future—as could be expected in their corporate capacity—but whether it was reasonable for them, when acting in a fiduciary capacity, to allow the Participants to invest their retirement savings in the Company's future as the Company's problems expanded and its prospects dimmed.

FACTS BEARING UPON DEFENDANTS' FIDUCIARY BREACHES

Overview

72. In June 2011, Arch bought International Coal Group Inc. ("International Coal") for approximately \$3.4 billion, expanding its metallurgical coal¹⁰ base and taking on significant

¹⁰ Metallurgical coal or coking coal or met coal is used in the process of creating coke necessary for iron and steel-making. Coke is a porous, hard black rock of concentrated carbon that is created by heating bituminous coal without air to extremely high temperatures.

Thermal coal or steaming coal is burned for steam to run turbines to generate electricity either to public electricity grids or directly by industry consuming electrical power (such as chemical industries, paper manufacturers, cement industry and brickworks).

debt. At that time, the metallurgical coal market was growing due to Asian demand. The international coal market appeared strong, but that appearance would quickly change.

73. On December 8, 2011, Goldman Sachs (“Goldman”) downgraded the U.S. coal sector from “attractive” to “neutral,” predicting electricity generators will continue switching from coal to natural gas through 2013.

74. Throughout the Relevant Period, as described in great detail below, while, experts and analysts saw little to no hope for the coal markets to rebound, Arch hemorrhaged money, and divested assets to maintain the liquidity necessary to survive long enough to ride out what it hoped was a short-term market cycle,¹¹ but what experts saw as likely a secular, or at least very-long term change, as its losses since 2012 are almost \$2 billion.

Quarter	Net Income / Loss (in millions)	Adjusted Fully Diluted EPS/LPS (Quarter)	Adjusted Fully Diluted EPS/LPS (year)
Q4'11	\$139.7	\$.29	\$1.07
Q1'12	\$1.2	-\$0.04	///
Q2'12	-\$435.5	-\$0.10	///
Q3'12	\$136.0	\$.20	///
Q4'12	-\$295.4	-\$0.42	-\$0.36
Q1'13	-\$70.0	-\$0.34	///
Q2'13	-\$72.2	-\$0.29	///
Q3'13	-\$128.4	-\$0.01	///
Q4'13	-\$371.2	-\$0.45	-\$1.08
Q1'14	-\$124.1	-\$0.60	///
Q2'14	-\$96.9	-\$0.46	///
Q3'14	-\$97.2	-\$0.45	///
Q4'14	-\$240.1	-\$1.09	-\$2.60
Q1'15	-\$113.2	-\$0.54	

¹¹ Even assuming, *arguendo*, that these hopes are objectively reasonable for the Company and its executives *qua* executives, they were unreasonable for ERISA fiduciaries when acting in their fiduciary roles.

The Coal Market Turns for the Worse, And Arch's Prospects Dim in 2012 as Experts Start to Talk about "Bankruptcy Red Flag Facts" Early in the Year

75. On January 20, 2012, FBR Capital Markets & Co. analyst Mitesh Thakkar lowered his outlook for coal prices to reflect softer-than-expected utility demand, weakening metallurgical coal exports and a potential for production curtailment by producers, and said there are "limited catalysts for PRB coal prices to rally in the near term."

76. On January 23, 2012, a *Wall Street Journal* article "US Coal Industry Losing Steam" reported that "[t]his year's outlook is grim for the U.S. coal industry, which after two years of rising profits has begun closing mines, signaling a new wave of production cutbacks and, possibly, another round of industry consolidation." The article quoted Brett Harvey, chief executive of Pittsburgh-based Consol Energy Inc., as recognizing that the industry is "entering a year with an unusual amount of uncertainty."

77. On February 3, 2012, an *SNL Daily Coal Report* article entitled "Coal executives trying to stay positive amid gloomy market conditions", reported that an industry conference the prior day reported that "[s]ome participants described the current market as gloomy, soft or even 'in the doldrums,'" and the mood was "certainly less upbeat than a year ago when metallurgical coal prices were at record levels due to supply shortages and surging demand from Asia."

Paul Reagan, president of Sampling Associates International, which specializes in the mechanical sampling of coal, remarked at the start of the conference that "it's hard to be an optimist." Reagan added, "You've got problems all over the place," including falling prices, coal production challenges at U.S. mines, a regime change in North Korea, Iranian nuclear ambitions and uncertainty over the United States' political future.

* * *

[Stifel Nicolaus coal analyst Paul] Forward noted that coal had other factors working against it, including tepid growth prospects for electricity generation in the U.S. and the increasing cost competitiveness of natural gas.

* * *

Despite challenges, John Eaves, Arch Coal Inc.'s president and COO, said that long term, he was "very bullish" on coal's prospects. Eaves said there are tremendous growth opportunities in the sector to serve export markets, with some 250 GW of new coal-fired generating capacity expected to come online globally by 2015. He estimated that there would be a global coal supply deficit of 300 million tonnes by 2015 if all the projects come online as scheduled.

Arch is developing a West Coast coal terminal to serve the booming Asian markets. Eaves said Arch is "very confident that [the terminal] will come online. It may be three, four, five years, but we think it will ultimately prevail."

Despite production cuts announced by some competitors, Eaves said, Arch remains committed to achieving its target of producing 15 million tons of metallurgical coal by 2015. And the company is expecting production of 19 million tons of met by 2017. "I think the current soft market will pass and brighter days are ahead," he said. Eaves declined to discuss any production curtailment that Arch might have planned ahead of reporting its fourth-quarter 2011 earnings on Feb. 10.

78. On February 5, 2012, the *Charleston Gazette* (West Virginia) reported that "[g]overnment experts continue to warn about an impending collapse of the Central Appalachian coal industry" and that "[t]he latest U.S. Department of Energy forecast says regional coal production may not decline as sharply over the next five years as previously projected, but cautions that the long-term outlook is even worse than initially thought."

79. Picking up on the gloomy market conditions recognized at the conference in Miami, on February 8, 2015, *TheStreet.com* reported in an article entitled "Trading Coal Stocks: Between Bankruptcy Risk and a Bottom" that:

The situation continues to look pretty bad for coal stocks, as it has since last year.

Low natural gas pricing and weak demand in a warm winter has kept a lid on coal. The steel market growth profile in 2012 and need for metallurgical coal is OK at best. These companies are in a

difficult balance sheet situation, but they've been here and done this cash crunch dance before. Smart investors often say to buy when there is fear in the market, and coal stocks have come back a little from October lows.

Is the next move closer to bankruptcy or an extended bounce?

First, the grim bankruptcy red flag facts.

Coal stocks are at significant balance sheet risk based on the Altman Z bankruptcy risk ratio, which was invented by New York University professor Edward Altman in 1968. The Altman Z-Score measures several aspects of a company's financial health -- including working capital, total assets, total liabilities, market capitalization, sales, retained earnings and earnings before interest & taxes (EBIT) -- to forecast the probability of a bankruptcy protection filing within two years. Since its inception, the formula has been 72% accurate in predicting corporate bankruptcies two years prior to the filing, according to Investopedia.

Companies with a Z-Score of 3 or higher are considered safe with little danger of bankruptcy, while those with a score of 1.81 or lower are considered distressed and are more likely to go bankrupt. Anything in between is a grey area.

Four key coal stocks all rate at a high risk of bankruptcy: **James River Coal, Patriot Coal, Arch Coal and Alpha Natural Resources**. The Altman Z score for these four companies has also been worsening in recent quarters, but this shouldn't come as any surprise as the coal stocks hit a valuation low in October:

* * *

Arch Coal: an Altman Z score of 0.86 vs. a score of 2.28 in the fourth quarter of 2010.

* * *

Arch Coal and Alpha Natural Resources both completed major acquisitions last year. Arch acquired International Coal Group and Alpha acquired Massey Energy. These deals have ratcheted up net debt at both companies, which has exacerbated the perceived bankruptcy risk. Net debt went from \$200 million to \$2.3 billion for Alpha from the fourth quarter 2010 to the third quarter 2011. At Arch Coal, net debt spiked from \$1.5 billion to \$3.7 billion.

Yet Alpha is sitting on \$600 million in cash, versus Arch with less than \$200 million in cash as of the end of the third quarter.

80. On February 10, 2012, Arch reported \$0.29 EPS for the quarter, missing the consensus estimate of \$0.31 by \$0.02. Arch has reported one profitable quarter since then, which profit was the result of a special charge and the cutting of expenses despite decreased revenue, as discussed below.

81. As *Dow Jones Commodities Service* reported in an article entitled “Arch Coal CEO: US Coal Miners ‘Face Some Headwinds’ In 2012” that Arch would cut production by more than 5 million tons this year, equal to about 3% of the company’s 2011 sales.

Many of the easy-to-access coal deposits in Central Appalachia have been tapped after more than a century of mining there. Arch said a “significant” portion of industry output from the region was losing money at today’s prices, and expects production in the region to drop by 20% this year.

82. Arch’s earnings quoted CEO Leer as stating

“Looking ahead, near-term market conditions have softened and we are reducing our planned production volumes to better align with weak generation and coal demand trends[.] These actions preserve our reserve base and increase our flexibility to respond as global and domestic energy markets evolve. At the same time, we will continue to maintain the development timetable for our metallurgical coal growth projects while generating positive free cash flow.”

83. Reporting on Arch’s outlook, on February 12, 2012, *The Wall Street Journal Online* posted an article entitled “Arch Coal to Rein In Production” which stated, in part,

Arch Coal Inc. reported a 48% rise in fourth-quarter profit on higher sales prices, but said it will rein in production because of softening demand.

* * *

Arch slashed its full-year adjusted earnings forecast twice last year, mostly on weaker-than-expected coal production at a West Virginia mine complex. To add to its production problems, the coal producer in November said it would cut up to 114 jobs at a Utah mine as it scales back production in response to the region’s continued weakness in coal demand.

Other coal companies made similar reductions amid softer customer demand. Alpha Natural Resources Inc. recently announced major coal production cuts, laying out plans to idle six mines and reduce output from four more, and Patriot Coal Corp. last month said it will idle five southern West Virginia mines to curtail higher production costs. Competition from cheap natural gas and depressed U.S. electricity use has pressured the sector, especially companies that operate high-cost mines in Appalachia.

84. On February 13, 2012, *The U.S. Coal Review* reported in an article about Arch's quarterly results that "Arch said it [i]s going to wade through the current market slump by controlling the cost aspects of its operations." In another article of February 13, 2012 entitled "The current market is bad but the good news is ... OK, there really isn't any" *The U.S. Coal Review* reported that "[b]arring something unforeseen, 2012 will be grim indeed where domestic utility coal consumption is concerned. The depth of the downturn could be staggering if a couple of major domestic steam coal consumers prove correct in their assessment of 2012 demand. The head coal buyer with a major Eastern utility said the loss of normal coal burn among utilities will be 'two to three times worse' this year than in 2009—yeah, 2009—unless conditions get unexpectedly better." The article also reported "[f]or the public companies, at least, 2012 'won't be a disaster,' one senior executive said. But he added that 2013 'is going to be the problem' if current market conditions persist. 'That's the point that's bad—if '13 isn't any better.'"

85. On February 14, 2012, a *Climate Spectator* entitled "US carbon rules could slam door on new coal plants" noted in part that the Obama administration was expected to soon unveil rules limiting carbon emissions from new coal-fired power plants and quoted Christine Tezak, an energy policy analyst at wealth management company Robert W. Baird & Co as saying that "[t]he proposed rule is certainly expected to send the message that *coal is dead*."

86. On February 20, 2012, *The U.S. Coal Review* reported in an article entitled "Arch says survival will be difficult for some high-cost suppliers as 2012" that

Arch says survival will be difficult for some high-cost suppliers as 2012 unfolds. The year is likely to be a very trying experience for many Central Appalachian coal producers, one fraught with lower sales, steep production cuts and the strong possibility of supplier casualties. While he believes Arch Coal will successfully manage its way through a brutal environment of low demand and low prices in the beleaguered region, company COO John Eaves opined that a number of less fortunate small-to-medium-sized producers might struggle mightily to keep their heads above water. With the cost of production in some cases now surpassing pricing for various CAPP coal qualities, trouble could be on the way for some lacking the staying power of the resource-rich big players like Arch. “That (*costs exceeding price*) is *happening now*,” Eaves said during Arch’s recent earnings call.

“I think it will be the process throughout the year. If you look at people’s cash cost in the current market, I don’t see how some of those guys survive. It will be tough. “*There is virtually no demand on the thermal side now.*” Arch CEO Steve Leer couldn’t agree more. He talked about the crushing obstacles blocking the path to prosperity for those struggling in CAPP. “I think this time there will be some shut down,” he said. “Having said that, coal miners are extraordinarily inventive and creative, and they can hang on longer than most people perceive sometimes. But you have to start to question. There is the regulatory environment. We haven’t talked about permitting for a long time, but there are permit issues hanging out there for a lot of producers. “It’s looking like a perfect storm. We could perhaps see a permanent reduction in production, particularly in the Central App region. This time I think there is a sense in the industry that the cost structure of production is such that some customer[s] are fearful that a lot of guys won’t make it, so they are turning their attention to companies like Arch.” The storm might damage Arch’s bottom line in the region for a while, but the pain won’t be as harmful as the hurricane-like destruction some producers might endure. . . .

87. On February 24, 2013, Arch declared a cash dividend of eleven cents per share to be paid to shareholders of record at March 5, 2012, on March 15, 2012.

88. On February 24, 2014, a *Dow Jones Factiva* article entitled “MARKETWATCH VIEW: Arch’s Stock Deserves Its Lumps Of Coal” that despite “attractive earmarks: reasonable stock valuation, a dividend yield above 3%, growing sales and all of the plusses of being an energy supplier” if you “[m]ine the data deeper and you’ll see that [Arch] stock is no diamond in

the rough, but it is the *Stupid Investment of the Week*” because it displays “conditions and characteristics that make a specific security *less than ideal for average investors*.”

The problem with Arch Coal, the nation’s second-largest coal producer, is that what looks attractive to the average investor is a bit of a mirage. The valuation and dividend yield look good in part because the stock got hammered last year, losing 57% of its value in 2011. That brings out bargain hunters thinking the company hasn’t got much further to fall, and hoping that a recovery to most fair-value estimates would result in a quick gain of 20% to 33%.

Unfortunately, a closer look at the numbers suggests that 2012 will be another rough year for the company, and that 2013 might not be much better. So even if the stock has the long-term potential for growth, the timing is wrong.

* * *

The balance sheet is a major concern, because it makes the company a bit more subject to the whims of the economy. That’s particularly true where the strategy of acquiring International Coal Group is involved, since that company was purchased largely because of its resources in the metallurgical coal business; metallurgical coal is a commodity where the price is heavily dependent on economic conditions in China, which could weigh on the company in the near term.

Further, U.S. coal prices currently are weak, and could be dramatically affected by how the government decides to regulate the business -- something industry insiders say could change depending on who wins the White House later this year.

Arch Coal has strong sales commitments for 2012 -- and its low-cost operations should ensure that it’s at least coming close to guidance levels -- but a quick look at the market could make some rethink their idea that coal is recession-proof; at the very least, it will make them recognize that coal is a commodity business, subject to all of the swings inherent to that description.

* * *

Put those things together and it’s clear why *analysts seem to hate Arch Coal right now*.

David Brown, chief market strategist for Sabrient Systems Inc., noted that *in the past month 90% of the analysts following Arch have lowered their estimates for the next quarter and/or next*

year, with much of the worry being the “aggressive accounting” on that stretched balance sheet. He rated the stock, at best, as a hold, which means he thinks more of it than most.

89. By this time, if not sooner, the Plan’s fiduciaries should have clearly known that Arch’s stock was not suitable for its employee’s retirement savings. Even priced efficiently, the Company’s shares were simply too risky for retirement savings.

90. On February 27, 2012, Arch announced that its chairman and chief executive officer, or CEO, Steven Leer will remain chairman of its board of directors but will retire as CEO, effective April 26, 2012, and that Leer will be succeeded by John Eaves, who served as its president and chief operating officer and as a member of its board of directors. Leer will remain with the company as chairman of the board of directors.

91. On March 1, 2012, speaking at the Coaltrans Coal Pricing and Trading conference in Geneva, Michael Hsueh, commodities analyst at Deutsche Bank said that on balance, “we think that global markets will either enter or maintain oversupply through the coming years and that affects our price outlook.” Hsueh also highlighted “higher than ever” pressure for US coal exports as a warm winter pushed gas prices down.

92. A March 12, 2012 article in *Platts Coal Outlook* entitled “Coal producers reaffirm ‘challenging’ 2012 at analyst conference” reported:

Some of the largest US coal producers shared their views on what is shaping up to be a tough 2012 at a two-day conference hosted by investment banking and equity research firm Brean Murray Carret & Co.

Brean Murray analyst Lucas Pipes, in a Monday report, said that one takeaway from the firm’s Global Resources & Infrastructure Conference on February 29-March 1 was that Central Appalachian thermal coal production could be drastically reduced in the coming years, by 60% from current levels, in the face of unprofitable markets.

* * *

“Our discussions generally confirmed our view that 2012 will be a challenging year for the group, while the long-term outlook for low-cost producers remains attractive,” Pipes said.

With respect to thermal coal, the market is expected to remain oversupplied in the near term, but current prices are not seen as sustainable, Pipes added.

* * *

“Arch Coal was bearish on Central Appalachian thermal coal demand. The company estimates that costs will continue to increase in the region. In addition, at current spot prices, essentially all of the thermal coal production is unprofitable. Without an improvement in the thermal coal market, the region’s thermal coal production could decline to just about 50 million tons over the coming years, down from 125 million in 2011,” Pipes said.

93. On April 25, 2014, 24/7 Wall St. reported that

Credit rating agency Standard & Poor’s [(“S&P”)]has put coal miner Arch Coal Inc. (NYSE:ACI) on CreditWatch with negative implications, threatening a one-notch downgrade to the company’s current ‘junk’ rating of ‘BB-’. S&P states the obvious:

Operating conditions for domestic producers of thermal coal and, to a lesser extent, metallurgical coal remain very difficult due to a mild winter, natural gas substitution in the U.S., and slowing steel production overseas. In our view, these conditions are likely to decrease demand and hurt contract pricing into 2013.

94. An April 29, 2012 article in *The Wall Street Journal Online* entitled “For Miners, Coal Is No Longer Hot” reported that “[i]t’s been a bleak spring for U.S. coal miners-and the question for Arch” is whether it can meet lowered expectations given that it was facing “some of the most challenging times that some of these coal companies have ever seen” according to Mark Levin, a coal analyst with BB&T Capital Markets (“BB&T”).

Whether [conditions will] get better anytime soon is an open question. Coal companies are facing what is expected to be a decades long shift in the way the U.S. generates electricity. A set of increasingly stringent federal air-pollution regulations-a much-delayed legacy of amendments to the Clean Air Act first enacted in

1990-are scheduled to come online during the next several years, pushing utilities away from coal and toward use of cleaner-burning fuels.

And this year, an unusually warm winter and spring limited electricity demand, while an unprecedented glut of natural gas made that fuel more attractive.

Weak demand has caused coal inventories to pile up at utilities to the point where some are delaying contracted deliveries.

* * *

Companies “are going to have to turn over every rock,” said Shneur Gershuni, an analyst with UBS.

Enough production cuts could eventually prop up domestic coal prices, giving producers something to cheer about later on this year.

Also, Arch, Alpha and the rest of the industry hope that increased coal demand from fast-growing China and India will help turn the tide. But that poses additional problems. U.S. companies are scrambling to increase their access to ports in the Gulf Coast and East Coast to ship coal abroad.

Arch’s and Alpha’s export outlooks, as well as sales forecasts for the higher-priced types of coal used in steelmaking, will be key to how investors view the industry’s prospects in the year ahead.

95. Also on April 9, 2012, *Platts International Coal report* reported that Bank of America Merrill Lynch had lowered its 2012 thermal coal price forecast, citing further downside risk on the back of physical oversupply unlikely to improve quickly and restrained demand. On the same day, *NGI’s Daily Gas Price Index* reported in an article entitled “Old Man Coal Getting Mugged by Cheap Gas” that coal volumes had declined steadily since late 2012 because low gas prices have caused utilities to switch away from coal.

96. On May 1, 2012, in an article entitled “Arch Coal 1Q Profit Drops On Weaker Demand, Higher Operating Costs” *Dow Jones News Service* reported that Arch’s first-quarter profit plummeted on weak demand and high operating costs.

“The U.S. coal industry is in the midst of a restructuring that will cause some players to exit the market and others, like Arch, to pare back operations until market conditions improve,” said Chief Executive John W. Eaves.

For the year, the company lowered its sales outlook by 15 million to 25.5 million tons, now seeing total thermal and metallurgical coal sales between 136 million to 142.5 million tons.

Shares were down 5.7% in premarket trading to \$9.20 as results missed estimates. Through Monday’s close, the stock was down 33% so far this year.

Like other U.S. coal companies, Arch had said it would cut production this year, as dirt-cheap natural gas prices continue to undercut coal’s competitiveness as a power source. An unusually warm winter added additional pressure.

Eaves said that with its low-cost mines and access to ports, the company is well-positioned to meet a growing global coal demand.

* * *

The company is increasingly looking abroad for profit. Arch Coal’s \$3.5 billion acquisition in June of International Coal Group expanded its production of metallurgical coal, which is used by steelmakers. In an effort to ratchet up exports, the company has arranged for additional port capacity in the U.S. and Canada, and opened offices in Singapore and London.

* * *

Total tons sold fell 1.9% from a year ago. The average sales price per ton increased 15%, offset by a 30% rise in operating costs per ton.

97. Reporting further on the Company’s results, a Dow Jones Factiva article entitled “Arch Coal CEO: Offsetting Lower Domestic Sales With Exports” stated, in part:

Longer term, the U.S. coal industry is facing what is expected to be years of declining demand from power plants as a set of stringent federal air pollution rules take effect in the coming years.

“We’ve really eliminated our exposure to the thermal markets” in 2012, Eaves said. The company expects to leave almost all of its planned, but unsold, thermal coal production in the ground instead

of trying to sell it into an already oversupplied U.S. market, executives said.

In the Appalachian region, Arch said it has cut 500 jobs since the market downturn began, closed five power-plant coal operations and curtailed output elsewhere. In the Powder River Basin in Wyoming, Arch limited shipments from Black Thunder, its largest mine, and plans to idle some equipment during the second quarter.

“We’ve put an aggressive plan in place to manage through the downturn,” Eaves said.

The company also announced plans to cut its quarterly dividend by 73% to 3 cents, saving around \$68.3 million a year. Arch had about \$117 million in cash and cash equivalents at the end of March, down from \$138 million a year earlier.

Arch said it also plans to refinance some debt, and cut its expected 2012 capital spending by about 10%

Shares were down 1.1% at \$9.65 as results missed estimates. Through Monday’s close, the stock was down 33% so far this year.

98. On May 2, 2012, 24/7 Wall St. reported that Fitch Ratings (“Fitch”) had lowered Arch’s credit rating to B+, four notches below investment grade, estimating that Arch’s free cash flow for 2012 will be negative, in the range of -\$150 million to -\$370 million and pointing to high inventories and high debt: Fitch also predicted weak earnings and high debt levels post the acquisition of International Coal would result in high leverage metrics over the period offset by strong liquidity.

99. *News Bites* reported on in a May 2, 2012 article entitled “Arch Coal hits year-low 20th time in three months” that

American company ARCH COAL INC. (ACC.F) hit a 52-week low in Germany of EUR6.95 during the day. In the last three months the stock has hit a new 52-week low twenty times, pointing to a significant downtrend. The stock price slid 38.0c (or 5.2%) to close at EUR6.95. Compared with the DAX index, which fell 50.4 points (or 0.8%) on the day, this was a relative price change of -4.4%.

100. On May 2, 2012, *Platts Coal Trader International* reported in an article entitled “Arch Coal to cut 2012 output on ‘severe weakness’ in US demand” that

Arch Coal will cut its 2012 production 25 million st below original projections due to “severe weakness” in US thermal coal markets, the company said Tuesday.

* * *

“The severe weakness in the US thermal coal markets impacted our first-quarter results and, consequently, we are resetting our 2012 expectations,” President and CEO John Eaves said in a statement. “Based upon an unprecedented build in power generator coal stockpiles year to date, the continued erosion in natural gas prices and relatively soft global metallurgical demand, we are further curtailing our production in 2012.”

Arch said in the first quarter it idled on dragline in the Powder River Basin, placed another into reclamation and “meaningfully limited” railcar loadings at its Black Thunder mine’s West Loadout. The company plans to have a total of three draglines and supporting equipment on idle in the second quarter.

In Appalachia, Arch said it delayed the startup of Mountain Laurel’s longwall in the first quarter following the successful transition to the Cedar Grove seam and closed five thermal operations and further curtailed production at other thermal mines. Since the market downturn, Arch subsidiaries have eliminated approximately 500 positions.

In the Western Bituminous Region, Arch said it has continued to rationalize supply at the company’s higher-cost mines.

In addition, Arch said it further reduced its discretionary capital expenditures by \$45 million and now expects to spend a total of \$410 million to \$440 million in 2012. The company also is evaluating capital spending plans in future years, including the potential delay of thermal coal replacement and expansion projects.

US coal industry ‘restructuring’

* * *

Arch said it now expects US coal consumption for power generation to decline by at least 75 million st in 2012 from 2011 levels, due to unfavorable weather trends that have reduced power

demand and contributed to a natural gas surplus. These factors have led to an increase in U.S. coal generator stockpiles to date in 2012, and internal estimates suggest that stockpile levels could peak at around 210 million tons by the end of May, before starting to reverse.”

101. On May 3, 2012, S&P lowered Arch’s corporate credit rating further into junk territory, to ‘B+’ from ‘BB-’, and lowered its senior unsecured notes rating to ‘B-’ from ‘B+’ and revising our recovery rating to ‘6’, which indicates our expectation for negligible (0%-10%) recovery in the event of default. S&P noted, in part, that the downgrade “reflects our expectation that 2012 and 2013 EBITDA will be much lower than previously anticipated because of a sharp cyclical downturn in domestic coal demand,” and that the rating reflects its view of the company’s “fair” business risk and its “aggressive” financial risk.

102. On May 8, 2012, Moody’s Investor Service (“Moody’s”) lowered its outlook on the fundamentals of the U.S. coal industry to negative, further expecting some of the decline in U.S. coal consumption to be permanent. Analyst Anna Zubets-Anderson said that “[a] regulatory environment that puts coal at a disadvantage, along with low natural gas prices, have led many utilities to increase or accelerate their scheduled coal-plant retirements.”

103. On May 14, 2012, *SNL Daily Coal Report* reported that Arch could be required to record a goodwill impairment charge of millions of dollars in the event that thermal or metallurgical coal markets weaken further, according to Arch’s Form 10-Q filed late on May 10.

104. On May 14, 2012, *SNL Daily Coal Report* reported in an article entitled “Analyst: Financial distress likely ahead for Central Appalachian coal miners” that

Barring an extremely hot summer that would force utilities to burn down swelling coal stockpiles and raise prices, Central Appalachian miners *Arch* Coal Inc. and Alpha Natural Resources Inc. ***could fall into financial distress in the next two or three years***, Morningstar reported.

The companies have both taken on tremendous leverage in making major acquisitions in 2011 and have considerable coal tonnage uncontracted for 2013. Should natural gas prices continue to fall, “we [foresee] coverage and leverage ratios deteriorating over the medium term,” Morningstar analyst Michael Tian wrote in a May 14 report.

“Given current production costs, we estimate that gas needs to rise to at least \$4.50 per thousand cubic feet before miners can produce coal and earn an adequate cash margin, which we set at \$10 per ton. Given current prices, the coal-to-gas switch will continue, albeit at a slowing pace, for the next several years,” Tian wrote.

* * *

In 2013, however, much coal remains uncontracted. Only about 40% of Morningstar’s estimated revenue for Arch is accounted for, and while Alpha does not disclose 2013 contract positions, “it’s a fair bet that very little of 2013 is committed and priced,” Tian said.

Morningstar predicts lower profitability for producers in 2013, with a gradual recovery in profitability beyond 2013. While Alpha and Arch produce higher-margin metallurgical coal in addition to thermal coal, Morningstar said, met coal prices have declined on evidence that steel demand from China may be slowing. Tian said global economic conditions could change quickly, but it assumed that the current pricing structure remains roughly intact.

“Although we assume a gradual recovery in profitability past 2013, ***the extremely high leverage ratios Appalachian miners should experience between 2012 and 2014 point to a material chance for financial distress for these companies,***” he wrote.

He noted that while Arch recently refinanced some debt at more attractive terms, its leverage ratios will remain high for several years and its free cash flow generation “will probably be quite anemic.”

105. A May 25, 2012 *SNL Daily Coal Report* article entitled “Goldman Sachs: Gas prices below \$3.50 make Illinois Basin, PRB coal vulnerable” reported that

Goldman Sachs said thermal coal producers face near-term headwinds from low gas prices but longer-term impacts due to upcoming air pollution regulations. According to the report, that will lead to the retirement of more than 57 GW of coal plant capacity as utilities decide against installing expensive pollution

controls to be compliant with new environmental regulations governing mercury and acid gas emissions. Most of those retirements are expected to come between 2014 and 2016. More than 33 GW of retirements have been announced to date.

Goldman Sachs estimated that 110 million tons of coal demand will be lost by 2018 from 2010 levels due to coal plant retirements. Based on a percentage of total coal production, the group estimated that the Interior region, which includes the Illinois Basin, will lose the most, with Central Appalachia and the Uinta Basin, which includes Colorado and Utah, not far behind.

106. A May 28, 2012, *Platts Coal Outlook* report entitled “Arch Coal shifts to export strategy in new document” stated in a recent analyst conference “shed light on [Arch’s] long-term plan to mobilize itself as the leader in the US export of thermal and metallurgical coals.”

“The key message from the analyst day was that Arch Coal is transforming to a major metallurgical coal and export thermal coal player from a predominantly domestic steam coal player before its acquisition of International Coal Group,” said Mitesh Thakkar, an analyst for FBR Capital Markets, in a research note published Thursday.

“Basically, we are saying that while the US market is likely to be slower growing, we still see significant opportunities here at home, particularly for the strongest and best positioned players,” said Arch spokeswoman Kim Link in a Friday email. “Meanwhile, we continue to ramp up our engagement in international markets where we believe there will be dramatic growth in the years ahead.”

In the document, “The New Arch Coal,” management estimates that seaborne coal volumes will double from 1 billion short tons last year to 2 billion st by 2020. And rather than doubling its export volumes to retain market share, Arch plans on more than quadrupling them.

In order to grow its export volumes from last year’s slog of 7 million short tons to about 30 million st by the end of the decade, Arch expects to gear its balance sheet toward capacity expansions at ports throughout the nation and grow its met production capacity.

* * *

Arch also doesn't think it will have to wait long until the higher met market pricing returns. Management points out that Chinese steel production has risen 3% this year through April.

107. On June 22, 2012, *SNL Energy Finance Daily* reported that Deck Slone, Arch's senior vice president of strategy and public policy, predicted that Arch had "turned the corner from getting worse in April and May to potentially beginning the long climb out," Slone said. "The stockpiles are starting to liquidate. Yes, those stockpiles cast a long shadow. But further out, we're optimistic. Longer term, there's a pretty compelling story for coal." The same article reported that "[t]he message from industry observers and executives is this: The short-term outlook for coal is dreary, and not every coal producer will survive. But if producers can withstand the next three to four difficult years, a more pleasant future awaits[.]" and concluded with "'There is light at the end of the tunnel,' Thorndike Landing LLC partner Olaf Karstens said. 'But it is not clear how long this tunnel is going to be.'"

108. Also in late June 2012, Arch announced that it planned to idle several operations and reduce production at other mining complexes in Appalachia due to the unprecedented downturn in coal demand. The slowdown was accompanied by a workforce reduction of approximately 750 full-time employee positions. *SNL Daily Coal Reports* reported on June 22, 2012, that Arch saw more consolidation in the coal industry as likely.

109. On June 22, 2012, an *Internal Business Times* article entitled "King Coal Has Lost Its Crown To Natural Gas (For Good), Despite Further Price Decline Forecast" reported

While coal has powered the 19th-century Industrial Revolution, heated homes and generated electricity, *the era of "King Coal" has come to an end.*

* * *

"The switch in fuel mix is here to stay and probably it's here to stay for a long time," said Rick Scott, senior managing director of L&S Advisors Inc.

* * *

This is an opportune time to switch from coal to natural gas.

* * *

“While power generation companies take advantage of the price difference, they at the same time also satisfy a lot of the environmental people, satisfy regulatory agencies and satisfy the administration to a certain extent,” Scott said.

While there will be some periodic price fluctuations in natural gas, Scott expects it could very easily fall below \$2 again.

And even if coal prices become ultra-cheap, as long as natural gas stays at the level it is today or lower, lower coal prices won’t necessarily outweigh all the other negatives that go along with it.

“There would be no incentives for utility companies to switch back to coal, as long as natural gas prices remain at these levels or even lower, irrespective of what the price of coal does,” Scott said.

Share prices of leading U.S. thermal coal miners, including Consol Energy Inc. (NYSE:CNX), Alpha Natural Resources (NYSE:ANR) and Arch Coal Inc. (NYSE:ACI) have all fallen significantly so far this year, with the latter two losing more than half of their value, respectively.

110. On June 27, 2012, Moody’s lowered Arch’s credit rating to B2, five notches into junk, or speculative-grade, territory, stating that it expects Arch’s credit metrics to deteriorate throughout into 2013 as sales remain low. Moody’s predicted challenging market conditions and industry-wide challenges would continue, and Arch’s credit metrics will suffer and its liquidity would deteriorate in 2012 due to challenging coal markets. Moody’s expected Arch to have sufficient liquidity during the next 12 to 18 months but expects its liquidity position to deteriorate. Moody’s also downgraded Arch’s senior unsecured debt to B3 from B2 and its secured credit facility to Ba3 from Ba2. The ratings affect about \$4.1 billion in outstanding debt.

111. On July 16, 2012 *Bloomberg News* reported that International Coal founder Wilbur Ross predicted the industry’s current slump differed from earlier setbacks and may last

for years because of the shale-gas boom. The article stated “Last time the cycle was this bad, the problems were essentially just cyclical,” Ross said in a July 10 e-mailed response to questions.

“This time the *major secular trends are far more likely to be unfavorable for years to come.*”

112. On July 27, 2012, Arch reported its Q2’2012 net loss of \$436 million, or \$2.05 per diluted share. Arch also declared a quarterly cash dividend of \$0.03 per share on the company’s common stock, payable September 14, 2012 to shareholders of record on August 31, 2012. On an analyst call of the same day, Company CEO Eaves recognized that “It has been a busy and challenging three months for Arch Coal. The year-to-date decline in coal demand has been unprecedented, yet we’ve been successful in executing on a plan to improve our operational efficiencies, optimize our asset portfolio and enhance our financial flexibility.”

113. In an August 7, 2012, presentation Arch offered a more pessimistic view for met coal than it had in May, but still projected a profitable long-term global met coal market.

114. On August 22, 2012 Moody’s predicted a rough 2013 for the U.S. coal industry.

115. On August 31, 2012, *SNL Daily Coal Report* reported that JPMorgan Chase & Co. downgraded the credit of Arch Coal Inc. to “neutral” and encouraged bondholders to take some profit, saying that metallurgical coal prices will continue to decline and the thermal coal market is unlikely to improve much in the near term. The same article reported that [JPMorgan analyst Dave] Katz expects Arch’s 2013 EBITDA “is likely to be drastically below current 2013 consensus forecasts of \$741 million. We believe consensus forecasts are likely to decrease over the next month or two, pushing bond prices down.”

116. On September 17, 2012, *Platts Coal Outlook* reported that Arch was idling its Imperial mine in West Virginia because of low demand. The mine was put on a “hot idle” status with many of its employees taking jobs at Arch’s Leer mine.

117. On October 3, 2012, *Platts Coal Trader* reported in an article entitled “Long-term [Powder River Basin (“PRB”)]outlook has downside: consultant” that

It’s not just the high-cost Appalachian coal region that critics are eulogizing anymore.

In fact, the low-cost Powder River Basin is the focus of a new study that predicts the basin is currently “experiencing a prolonged declining domestic market.”

John Hanou, principal consultant at Hanou Energy Consulting, released his new study, “Powder River Basin Coal Supply, Demand & Price Trends 2012-2031,” on Tuesday.

About one year ago, Hanou released a report on the long-term advantages of the Illinois Basin. Now with his eye trained on the PRB for the past year, his viewpoint is much less upbeat.

While he expects domestic PRB demand to rise by about 30 million short tons in the short term, Hanou expects overall demand to drop by a net 50 million st/year by 2024.

“By 2025, about 80 million st/year [worth of PRB-burning plants] will be retired,” Hanou said in an interview. “Most are happening prior to 2020. About 40 to 50 million st of new build demand and about 14 million st of decline from Canada” is how he arrived at the net 50 million st/year decline.

* * *

With its Black Thunder mine production already reduced by about 25 million st this year, Arch Coal’s chief PRB mine is in a difficult position as well, Hanou said. To continue close to 100 million st/year by decade end, it will need to move as much as 800 million cubic yards of overburden, he said.

118. On October 8, 2012, Analysts at Morgan Stanley initiated coverage on shares of Arch in a research report issued to clients and investors on Monday. The firm set an “underweight” rating and a \$3.50 price target on the stock. Morgan Stanley analyst Evan Kurtz said cheap natural gas and latent thermal coal capacity due to mine idlings have created long-term structural headwinds in the thermal coal market offering limited sustainable upside for

thermal coal prices. It also said that while coking coal prices might rise, Arch's coking coal mix is skewed to lower-quality products, which achieve lower margins.

119. On or about October 9, 2012, Goldman downgraded Arch from Neutral to Sell and reduced its price target from \$7.50 to \$5, noting:

We lower ACI to Sell from Neutral, as we see shares as overvalued given fundamental and strategic challenges. We expect met coal guidance to be reduced. We see 22% downside to our \$5.00 six-month multiples-based target price, down from \$7.50, vs. 13% upside for the rest of coverage. We see shares as overvalued given a weak balance sheet/returns and strategic challenges.

120. On October 25, 2012, Arch declared a quarterly cash dividend of \$0.03 per share payable December 14, 2012 to shareholders of record on November 30, 2012.

121. On October 26, 2012, Arch reported its third quarter 2012 results. The Company's earnings release included the following:

"Looking ahead, we believe global coal markets are in the process of correcting - with the domestic thermal market building some momentum while metallurgical markets are bottoming out," said Eaves. "Because we expect global coal market conditions to remain challenging in 2013, Arch is executing a strategy to successfully navigate this weak market. Our plan is focused on improving operational efficiency, optimizing our asset base and preserving liquidity so we are well positioned to capitalize as the market recovers."

Executing Our Plan "We are prudently matching our production levels to market demand, reducing costs and lowering capital spending," said Paul A. Lang, Arch's executive vice president and chief operating officer. "We anticipate that 2013 will be a difficult year for the coal industry, but we believe our ongoing efforts will allow Arch to emerge from this cyclical downturn as an even stronger company."

122. *Zacks Investment Research* reported in an article entitled "Arch Coal Posts Mixed Result - Analyst Blog" that Arch

reported pro forma earnings per share of 20 cents in third-quarter 2012, significantly beating the Zacks Consensus Estimate of a loss

of 15 cents per share. Quarterly results were also higher than the year-ago earnings of 3 cents per share.

Arch Coal's growth in quarterly earnings was driven by a decline in its cost of operations including reduction in depreciation, and selling, general and administrative expenses.

* * *

Total Revenue

Arch Coal's total revenue in the reported quarter was \$1,087.6 million, down from \$1,198.7 million in the year-ago quarter. Quarterly revenue fell short of the Zacks Consensus Estimate of \$1,033.0 million.

The company's third-quarter 2012 revenue decreased primarily due to a decline in average sales price per ton to \$25.57 from \$27.87 in the year-ago quarter. This was partially offset by an increase in shipments in Arch Coal's western operating regions.

Operational Update

Arch Coal sold 37.5 million tons of coal in third-quarter 2012, down 6% from the year-ago level of 39.9 million tons. This decrease in sales volume resulted from sales volume decline in Powder River Basin (PRB) and Appalachia; partially offset by an increase in sales volume at Western Bituminous Region.

The company's adjusted earnings before interest, tax, depreciation and amortization (EBITDA) in third-quarter 2012 were \$256.5 million, up from \$211.5 million in the year-ago period.

Interest expenses were \$74.3 million at the end of the third quarter of 2012 compared with \$76.9 million in the prior-year period.

Financial Update

Cash and cash equivalents of the company as of September 30, 2012 were \$550.8 million versus \$138.1 million as of December 31, 2011.

As of September 30, 2012, Arch Coal's long-term debt was \$4.5 billion compared with \$3.8 billion as of December 31, 2011.

In the first nine months of 2012, the company's capital expenditure was \$304.0 million compared with \$215.9 million in the prior-year comparable period.

Guidance

In 2012, Arch Coal expects to sell 129 - 135 million tons of thermal coal and 7.5 million tons of metallurgical coal.

Selling, general and administrative expenses are expected to be in the range of \$125.0 - \$135.0 million in 2012.

Interest expenses are expected to be in the range of \$300.0 - \$310.0 million in 2012.

For full-year 2012, the company's capital expenditure will likely be in the range of \$410.0 - \$430.0 million.

* * *

Our Take

We have observed that Arch Coal continues to follow several cost reduction measures including idling of three of its mines in Appalachia to manage current market demand. The company also plans to reduce its capital spending on low return units. These initiatives will enable the company to improve its forthcoming financial as well as operation results.

In addition, Arch Coal intends to expand and develop its low-cost asset portfolio by constructing the high-quality Leer metallurgical coal mine in the region. The company expects Leer mine to contribute substantially to its top line in future.

However, we believe that these growth opportunities could be challenged by softened global and U.S. coal demand, which will influence Arch Coal's financials in the following quarters. Secondly, increasing substitution of coal with natural gas could drive down coal prices while impacting the company's margins.

123. As *24/7 Wall St.* reported in an October 26, 2012 article entitled "Arch Coal Reports Surprise Profits",

Arch Coal's rather stunning results are the result of strict cost control. The company has shut down three mines and expects to lower its forecast capex spending by \$60 to \$80 million for the full fiscal year.

The company believes coal consumption will grow again in 2013 as natural gas costs rise above \$4 per million BTUs. That is roughly equivalent to \$32 a ton for bituminous coal. Arch reports

commitments to sell its western bituminous coal at \$35.75 a ton in the fourth quarter at a cash cost of \$23.00 to \$25.50 per ton. Powder River Basin coal is committed at \$13.63 a ton after a cash cost of \$11.00 to \$11.30 a ton.

124. Another *24/7 Wall St.* reported in an October 26, 2012 article entitled “Is Arch Coal a Buy after Strong Earnings?”

According to the EIA, the U.S. exports about 7.5 percent of coal produced. If a recovery is imminent, that number will need to rapidly increase. Domestically, there may also be a shift how much of coal produced is used for electric power versus industrial purposes. If natural gas edges coal out of power plants, we could see a higher percentage of the production mix going to coke plants.

Based on the metrics, Arch Coal is a Stay Away. Despite surprising investors across the board today with solid earnings, there is no guarantee that the company can make a healthy comeback. If the coal industry does come back, it is more likely that larger players like Peabody (NYSE:BTU) will take the lead. Going long, growth will come from natural gas and renewable sources.

125. Also in response to the only quarterly profit the Company would turn in from Q2’2012 through the end of 2014, SNL Daily Coal Report noted in an article entitled “One-time benefit boosts Arch’s Q3 earnings, but 2013 to be ‘difficult’” that

Maneuvering through tough coal market conditions, Arch Coal Inc. on Oct. 26 reported third-quarter earnings that were well ahead of a year ago, but the results were largely due to a one-time, legal-related benefit.

* * *

Arch noted that its third-quarter results included an \$80 million benefit from the reversal of a previously recorded legal contingency, or \$54 million when adjusted for taxes and previously accrued interest expense.

* * *

The challenges on the pricing front will likely linger into 2013, as Arch officials said they anticipate next year being a difficult one.

“We are prudently matching our production levels to market demand, reducing costs and lowering capital spending,” COO Paul Lang said. “We anticipate that 2013 will be a difficult year for the coal industry, but we believe our ongoing efforts will allow Arch to emerge from this cyclical downturn as an even stronger company.”

Eaves added that “because we expect global coal market conditions to remain challenging in 2013,” Arch intends to continue its focus on improving operational efficiency, optimizing its asset base and preserving liquidity so it is well-positioned to capitalize when the market recovers.

Leer mine ships first coal

Part of Arch’s plan to focus on its most efficient assets is the continued development of its new Leer mine, which shipped its first train of coal on Oct. 23, with the shipment bound for customers in Europe. The company has a continuous miner unit operating at the West Virginia metallurgical coal mine, and it anticipates starting up the longwall at Leer in the third quarter of 2013.

Formerly known as the Tygart Valley No. 1 mine, Leer ultimately is targeted to produce 3.5 million tons of high-quality met coal annually. Arch acquired the mine through its acquisition of International Coal Group Inc.

Arch said it also is emphasizing cost control at its mines by ongoing efforts to improve operational efficiencies across all regions, as well as by increasing shipment levels from its lower-cost operations in the Powder River Basin and the western bituminous region.

The company also is reducing planned capital expenditures, saying it now expects capital spending of approximately \$350 million for 2013, below its estimated 2012 capital spending range of \$410 million to \$430 million.

126. On November 8, 2012, Goldman reduced its outlook on the U.S. coal sector to “neutral” and urged investors not to “buy the dip” in coal stocks on its view that a modest recovery in demand for thermal coal and metallurgical coal appears to be priced into the stocks. Goldman noted a “sell” rating on Arch.

127. On November 13, 2012, as reported the next day in an *SNL Daily Coal* reported entitled “Arch Coal to boost liquidity in preparation for delayed market recovery” that

Arch Coal Inc. . . . said it plans to boost liquidity by issuing senior notes and taking out a term loan that, together with existing balances, will give it cash and marketable securities of more than \$1.2 billion and help it prepare for an extended market downturn.

The company commenced a private offering of \$350 million of senior notes due 2019 that will be guaranteed by its subsidiaries. Additionally, Arch has launched a \$250 million senior, secured term loan due 2018 to replace some capacity from the company’s revolving credit agreement. Proceeds from the offering of notes and term loan will be used for general corporate purposes.

Completion of the new term loan will reduce the company’s revolver to \$350 million from \$600 million, Arch said. The company also is planning to seek additional flexibility under financial covenants governing the revolver.

“We are proactively executing a comprehensive financing plan aimed at boosting our cash on hand, enhancing our overall liquidity and maintaining our financial flexibility,” Arch President and CEO John Eaves said in a news release. “This plan provides Arch with excess liquidity in case the current market weakness lasts longer than expected, and adds long-term, pre-payable debt to help the company achieve its de-levering goal as markets recover.

“Metallurgical coal markets remain challenged at present despite some improvement in global and domestic thermal markets,” Eaves said. “In light of the weak environment, Arch has been successfully pursuing a plan to improve operational efficiency, reduce capital spending and bolster available financial resources. We believe our proactive plan will ensure that Arch is well positioned as an even stronger global resource provider when coal markets rebound.”

Earlier in 2012, rating agencies reduced their rating on Arch’s corporate credit, citing liquidity pressures faced by the company as it struggles to weather the coal market downturn with a heavy debt load. At Sept. 30, the company’s long-term debt was almost \$4.47 billion, according to its Form 10-Q filing.

128. On November 13, 2012, in response to its debt changes, Fitch downgraded Arch’s credit ratings another notch to B, five steps into junk territory, from B-plus with a negative

outlook, because of concerns about high leverage. The negative outlook reflected the potential that weak market conditions could drag into 2014.

129. Similarly, on November 14, 2012, S&P lowered its outlook on Arch to negative, amid expectations that Arch's borrowing plans will push leverage much higher. S&P affirmed Arch Coal at B-plus--four notches into junk territory--partly on its expectations the industry may have hit its cyclical trough and that the company's strong liquidity will enable it to withstand a difficult market if weak conditions persist for an additional year or two. Arch and its rivals have been hurt by low natural-gas prices in the critical power-generation market.

130. A *U.S. Coal Review* article entitled "Arch moves on comprehensive financing plan while awaiting market recovery" reported on November 19, 2012 that

Arch moves on comprehensive financing plan while awaiting market recovery

Arch Coal has launched a \$250 million incremental, senior secured term loan due 2018, pursuant to an uncommitted accordion provision in the company's existing revolving credit agreement.

Completion of the new term loan offering would reduce the size of the company's revolving credit facility to \$350 million from \$600 million. Concurrent with the term loan offering, Arch announced that it has commenced a private offering of \$350 million in senior unsecured notes due 2019.

Arch intends to use the net proceeds from the offering of the senior notes and the term loan for general corporate purposes. Upon completion of its efforts, Arch expects to have a cash and marketable securities balance in excess of \$1.2 billion.

Separately, Arch plans to seek certain amendments to its secured revolving credit facility to provide additional flexibility under the financial covenants that govern the facility. The completion of the offering of senior notes is not conditioned upon the success of amending the revolving credit facility, nor are any consents required to complete the offering.

131. Two weeks after increasing its debt load, *Platts Coal Outlook* reported in a December 3, 2012 article entitled “Arch Coal focused on reducing debt: CEO”

Arch Coal CEO John Eaves said Wednesday that he is focused on paying down the company’s debt.

Speaking at the Jefferies 2012 Global Energy Conference in Houston, Eaves said his main concern in a rough market like 2012 has been to reduce costs, including debt payments, rather than focusing on growth.

“The focus near term is deleveraging our balance sheet, period,” Eaves said.

The company had long-term debt of \$4.5 billion at the end of the third quarter, SEC filings show.

Once the company is suitably deleveraged, Eaves said he would begin looking at “organic or strategic” growth options. While he didn’t specify a particular level of debt reduction, Eaves was optimistic that Arch would begin paying down \$600 million of long-term bonds with 2016 maturities when they become qualified for early repayment in August 2013.

“On the capital side, I don’t think it’s any secret that we’ve been in a pretty challenging environment over the last six to twelve months,” Eaves said. He said the company is forecasting a \$350 million range for capital spending in 2013, far below the company’s typical spending in recent years, and continues to work on cost containment measures.

If the market improved in the latter half of 2013, Eaves said Arch would deleverage much more quickly. He predicted higher natural gas prices and falling utility stockpiles would aid the market rebound in the latter half of next year.

132. On December 12, 2012, a Fitch special report entitled “2013 Outlook: U.S. Coal Producers” highlighted trends in the coal industry, such as high coal and natural gas inventories, economic weakness in Europe, and cost inflation. It predicted those factors would severely limit industry recovery before 2014, Fitch did not expect relief from cost headwinds over the next 18 - 24 months and noted that recent debt-financed consolidation had strained balance sheets.

133. In a December 28, 2012 research note, Goldman predicted U.S. coal companies will lose 8% on average in 2013 as a “recovery cliff” looms, bringing multiyear declines in metallurgical coal exports and falling thermal coal demand and that longer-term changes in the market “make[] coal stocks unlikely to have sustained outperformance.” Noting overvaluation on weaker fundamentals than its peers, Goldman retained its “sell” rating on Arch.

Facing a Grim Outlook, Arch Muddles Through 2013 Hoping for a Coal Market Recovery

134. In a Jan. 9, 2013, sector outlook report, Credit Agricole analyst David Lipschitz estimated that utilities will need to burn an additional 60 million tons of coal from inventories in order to bring them back to the year-ago level and without that additional burn, 70 million tons of coal production would have to be taken offline to compensate for the inventory overhang.

135. On February 5, 2013, Arch reported its fourth quarter and full year 2012 results. In response to the Company’s announcement, the *St. Louis Post-Dispatch* (Missouri) reported in an article entitled “Arch Coal posts huge loss; shares battered” that

Investors pummeled Arch Coal Inc. shares Tuesday after the company delivered a steep fourth-quarter loss that reflects a continued decline in coal demand and prices.

The \$295.4 million loss equaled \$1.39 a share, compared with net income of \$70.9 million, or 33 cents a share, a year earlier. Sales slid 21 percent to \$968.2 million as Arch shuttered mines, idled equipment and laid off hundreds of workers amid the deepest industry slump in years.

The cutbacks led to a 15 percent decline in Arch’s sales volumes. Realized coal prices during the quarter also fell 7 percent to about \$24 a ton.

Arch and other domestic coal miners have curtailed spending and idled unprofitable mines as demand falls in response to competition from abundant natural gas and the shutdown of older coal-burning power plants.

Sales of so-called metallurgical coal used by steelmakers have also been slowed by a sluggish global economy.

“While it’s never fun at the bottom of the market cycle, we as a company have been here before, and we know what it takes to manage through the trough,” John W. Eaves, Arch’s chief executive, said during a conference call with analysts and investors.

Excluding an asset write-down that comprised the bulk of the loss and other nonrecurring costs, Arch lost \$88.7 million, or 42 cents a share. On that basis, the loss was wider than the 14-cent average of analysts surveyed by Bloomberg.

Arch shares fell 13 percent to \$6.04 a share on the New York Stock Exchange.

Executives painted a somewhat brighter picture for 2013, particularly for the second half of the year.

But they said the timetable for a coal market rebound is anything but certain, and Arch plans to further reduce capital spending.

The executives also said sales volumes of 133 million to 144 million tons is substantially the same as the 140 million tons produced last year.

136. Also on an analyst call of February 5, 2013, Company CFO John Drexler recognized that “we are beginning to see some signs of improvement in coal markets. However, the timing and magnitude of a recovery remain uncertain.”

137. On February 6, 2013, the *International Business Times* (US ed.) reported in an article entitled “Coal’s Darkest Hour: Fitch Warns Of Increased Bankruptcy Possibilities in US Coal Sector” that declining demand, competition from natural gas, a weaker economy and tough environmental rules had combined to hit coal producers hard. The article also reported that “some coal companies are doing somewhat better than their peers” and listed three such companies, not including Arch, “that are managing their way through the down cycle with limited default risk[.]”

138. On February 9, 2013, *Zolmax.com* reported that Arch had been downgraded to “Neutral” at JPMorgan Chase and

JPMorgan Chase cut shares of Arch Coal (NYSE:ACI) from an overweight rating to a neutral rating in a research note issued to investors on Wednesday. The firm currently has \$7.00 target price on the stock, down from their previous target price of \$10.00.

“Declining met coal prices were the primary driver of \$231m in write-downs as new CEO John Eaves prepares the company for a difficult H1 2013 and hopes for a H2 recovery. We estimate the company will generate \$404m of EBITDA in 2013 and could come close to its senior secured leverage covenant of 3.5x risking dilution. With about 30mt of spare production capacity in the PRB, we are concerned that coal prices could be capped and this makes ACI vulnerable if the coal price recovery is delayed.” JPMorgan Chase’s analyst wrote.

139. A February 11, 2013 *The U.S. Coal Review* article entitled “PRB producers could spend the year just trying to hold on to market they” reported in part

The numbers are still being finalized but the PRB produced about 40 million tons (give or take a million tons) less in 2012 than it did in 2011. “It will be a challenge to find the markets to produce more this year,” the source said. “That doesn’t mean it won’t happen, ***there just is not a reason to think that it will happen.***” Anyone who has ever played any kind of game knows that sometimes a tie is the best you can hope for, and this year in the PRB that could be the case. “Any gains (in prices) are likely going to come after the first half of the year and it wouldn’t most likely be until the fourth quarter,” the source said. “But I think if we can just hold our ground this year, 2014 should get things going back in the right direction. I think you will see that’s the position of a lot of companies. Hold your ground for now and work on the out years a bit more.” What makes the out years look a bit better is while the U.S. coal industry wrestles with its own government over the future of coal—I tie would be great in that match, too—the rest of the world is expected to ramp up its coal use. Without getting into the will-they, won’t-they-be-built discussions of export terminals, if the rest of the world is burning more coal it’s likely to be a case of a rising tide lifting all boats. “I think the big chore this year will be controlling costs to make sure that we’re competitive going forward,” the source said. “Costs went up in all the basins last year, but I think most companies—in a bad market—are saying ‘We can’t control the market, but we can control how much we’re spending when the market comes back.’” A point that was hit on by Arch Coal during its fourth quarter earnings call is they have been able to take advantage of the downtime in mining—Arch said it has two draglines, eight shovels and related equipment idle as of

now—to get a jump on reclamation work. The source said it’s a plan that other companies are following that will pay off down the road although it doesn’t do much to make the current bottom line look better. “We’ve got the people available to get the work done now, so why not?” he said. “It’s not something that looks good on the bottom line today, but when the market comes back you’re actually cutting some future costs by getting that work done now.”

140. On February 14, 2013, Arch declared a quarterly cash dividend of \$0.03 per share of common stock, payable March 15, 2013 to shareholders of record on March 1, 2013.

141. A February 14, 2013 article in *SNL Daily Coal Report* entitled “BB&T: Investors spooked by Arch Coal’s contracting PRB coal below cost” reported that

BB&T Capital Markets said the steep sell-off in Arch Coal Inc. common shares Feb. 5 was probably due to the company’s disclosure that it priced millions of tons of Powder River Basin coal for delivery in 2013 ***“well below its cash cost.”***

“To be fair,” wrote BB&T analyst Mark Levin in a research note Feb. 12, “the company was able to lock in well-above-market prices for 2014, but [the sell-off] underscores how investors, who desperately want to like the PRB for its low-cost structure/mining dependability/low breakeven price vis-a-vis gas, continue to wonder if pricing can ever take off again if producers don’t leave more tons in the ground.”

Arch disclosed that it contracted more than 16 million tons of PRB coal for 2013 delivery at \$10/ton, compared to estimated cash costs of \$10.75 to \$11.50/ton, Levin said. “While management noted the strikingly low price included the impact of weak export prices and lower-grade coal, the conclusion reached by many was that [Arch] was willing to commit tons at prices well below their all-in cost ... in order to (a) keep their assets sweating given the high fixed-cost nature of the business, and (b) secure higher prices for 2014 and beyond.

“What’s clear from the numbers and conference call is that [Arch] made a business decision that has caused many in the investment community to scratch their heads,” Levin said, and he raised questions about whether Arch is concerned about losing market share to competitors.

* * *

In an earnings conference call, Arch officials said a rapidly changing global marketplace for coal that is opening doors internationally while closing them domestically necessitated the sale of PRB coal below cost. Arch President and CEO John Eaves said that despite low coal prices, the company needs to build business relationships with export customers now in the face of flat U.S. demand for its Powder River Basin coal. “If we’re going to grow, we have to look at that market, and we can’t wait a year or two down the road for markets to improve to be part of it. ... We don’t like the prices either, but we do think strategically it’s important to do that now versus wait.”

142. A February 14, 2013 article in *SNL Daily Coal Report* entitled “Arch sees Central App thermal market collapsing; idled mines unlikely to return” reported that

Arch Coal Inc. CFO John Drexler said Feb. 26 that the company expects Central Appalachia coal production to total less than 130 million tons in 2013, down from about 185 million tons in 2011, due to a “collapsing” thermal market for the high-Btu coal.

Drexler said at the BMO Capital Markets Global Metals & Mining Conference that Arch closed 10 complexes in the region, mostly higher-cost thermal operations.

“Quite frankly,” he said, “we don’t see those coming back in the near term.”

143. A March 1, 2013 *Platts Energy Economist* article entitled “US coal takes early retirement” reported that “US coal is under pressure, and not simply because of new environmental regulations. The 50-year old plus, tail end of the US coal fleet is uneconomic in any regulatory scenario, while natural gas has supplanted coal as the country’s number one energy commodity” and “[t]he structural shift in the US generation fleet away from coal towards gas and renewables appears largely unstoppable.”

144. A March 5, 2013 *Wall St. Cheat Sheet* article entitled “Will Arch Coal Inflict Unbearable Pain on Investors?” reported that

That’s an ironic question in the title, considering the fact that Arch Coal has already inflicted unbearable pain on investors. However, it’s not where you’ve been, it’s where you’re going, right?

It's definitely true that Arch Coal had some blunders over the past few years. After figuring out that Central Appalachia wasn't the place to be and focusing more on the West, Arch Coal acquired International Coal Group, which led to a refocus on Central Appalachia. This increased debt limited Arch Coal's ability to maneuver, and now it's stuck in a situation where it must deleverage prior to being able to grow again. This means more short-term pain. Will there be better times ahead? And considering the weakness in the industry over the past few years, would Arch Coal have been stuck anyway? The answer to the latter question is most likely yes.

* * *

The debt-to-equity ratio for Arch Coal is considerably weaker than the industry average of 0.70. The balance sheet is in negative territory. Operating Cash Flow is \$332.80 million. Levered Free Cash Flow is \$6.33 million. These aren't very impressive numbers, but they could be much worse, and Arch Coal is determined to make improvements.

* * *

Conclusion

Arch Coal has weak margins, weak cash flow, poor debt management, and it's in an industry that's hurting at the moment. It's very possible that the company's stock will continue in free-fall mode, especially if the economy (or stock market) turns for the worse. That said, Arch Coal is still the second-largest coal producer in the United States, and with increased demand likely to come from emerging markets, Europe, and Japan, Arch Coal is likely to benefit. It's also possible that natural gas won't remain as favorable in the United States as it is now. However, this might take a few years and a new U.S. president.

145. An April 16, 2013 article in *SNL Daily Coal Report* noted that analysts at Citigroup analyst Brian Yu cut his ratings for Arch to "neutral" from "buy," with a \$6 price target (lowered from \$9) saying that its valuation looks less attractive under Citi's new met coal forecast. Citi reduced its 2014 price forecast for hard coking coal used in steelmaking by 11% to \$190/tonne. Yu said the shorter-term outlook for met coal looks worse with the third-quarter

2013 benchmark pegged at \$165/tonne, which is better than current spot prices but below the most recent international settlement of \$172/tonne.

146. On April 23, 2013, Arch reported its first quarter 2013 results. Reporting on the same, a *Benzinga* article entitled “Arch Coal Trades Down on Sooty Revenue” reported

Arch Coal [] is down on Tuesday after posting woeful first-quarter sales.

* * *

Arch’s Appalachia segment’s sales volume decline 24.5 percent to 3.4 million tons. And, its average sales price per ton in the region dropped 14.4 percent, piling on to its woes in the Eastern US.

The coal mining firm’s sales volume also dropped in the Powder River Basin region of Montana and Wyoming, falling 2.2 percent to 26.6 million tons. Prices in this segment declined 8.6 percent.

Meanwhile, the nation’s second-largest coal producer’s Western Bituminous Region was the lone bright spot, with its sales volume growing six percent to 3.5 million tons. As with the other segments, though, prices declined, albeit by a modest 3.4 percent.

* * *

US Coal Market to Improve?

According to President and CEO John W. Eaves, ‘Positive catalysts, such as normalized weather and higher competing fuel prices, are improving the outlook for the domestic thermal market, our largest market by volume. We expect these trends to continue to reduce customer coal stockpiles throughout 2013 and to create a more balanced U.S. coal market thereafter. Globally, we believe metallurgical and thermal coal markets are in the process of stabilizing, and we anticipate gradual improvement as we progress through the remainder of the year.’

Eaves also stated, ‘The trend in U.S. coal markets is improving. U.S. power demand is rising in 2013, coal production continues to rationalize, and coal is regaining its share of the domestic power generation market due to the higher cost or lack of availability of competing fuels.’

Hazy Outlook

Arch hasn't offered any specific EPS or revenue estimates, but it anticipates selling 133-144 million tons of coal during fiscal 2013. At the middle-ground of 138.5 million tons, it would fall short of the 140.7 million tons it produced in 2012.

Black Day on Wall Street

On word of its revenue woes, Arch is down big in the early hours of trading. The stock is falling toward \$4.50 as of this writing after closing at \$4.89 on Monday.

147. On a first quarter analyst call on April 23, 2013, CEO John eaves stated that "[i]n summary, Arch is managing what it can control. We can't predict when prices will improve but we are seeing signs that markets are correcting and we're ready to capitalize as the cycle turns."

148. On May 10, 2013, Fitch lowered Arch's credit ratings by one notch to B-minus, six steps into junk territory, with a negative outlook. The downgrade cited oversupply in the U.S. steam-coal market that was likely to lead to significantly weaker earnings. Fitch also predicted lower earnings, combined with high debt levels after the acquisition of International Coal, as leading to high leverage metrics over the ratings horizon, and said it expected Arch's financial leverage to remain elevated until industry-wide production cuts have resulted in more balanced steam and metallurgical coal markets.

149. On June 7, 2013, the *Associated Press* reported that Arch would scale back operations at two coal mining complexes in Kentucky and Virginia, trimming the work force by more than 100 because of "ongoing coal market challenges." The two complexes affected were the Cumberland River complex and Hazard complex, both in Kentucky.

150. A June 7, 2013 24/7 Wall St. article entitled "Coal Mining Stocks Downgraded; James River Hit Hardest" reported in relevant part that Arch had been downgraded to underperform and that

The coal miners are caught in a real dilemma. Low coal prices need to fall even further to force the miners to cut production even

more. . . . Prices for met coal haven't yet reached a bottom, which means that prices will remain low for a longer time than many observers believed. For coal companies laden with debt, this means refinancings and all the added costs associated with that.

151. On June 14, 2013, *St. Louis Business Journal* reported in an article entitled "U.S. coal exports drop in April" that

U.S. exports of metallurgical grade coal, which is used in steel making, dropped from \$859 million in March to \$648 in April, a 25 percent fall-off, according to the most recent data from the U.S. Census Bureau. The figures are seasonally adjusted.

U.S. exports of coals and fuels dropped 34 percent to \$534 million in the same period.

Although St. Louis-based Arch Coal recently opened an office in China, and experts expect global steel manufacturing and global demand for metallurgical coal to increase in the second half of this year, it hasn't happened yet.

"The industry has found itself in a position where there's a tremendous oversupply," Ernie Thrasher, chief executive of XCoal, a U.S. coal trader that works on behalf of U.S. producers who want to sell coal in Asia, told the Wall Street Journal.

He is now forecasting U.S. coal exports to decrease 10 to 15 percent this year.

That's bad news at struggling St. Louis-based Arch Coal, Patriot Coal and Peabody Energy. Arch Coal (NYSE:ACI), led by President and CEO John Eaves, which recently cut more than 100 jobs at two of its mining complexes, posted a loss of \$683.7 million on revenue of \$4.16 billion in 2012. . . .

152. On June 28, 2013, Arch announced that it would, as part of an ongoing strategic review aimed towards lowering debt and paring down assets, sell wholly owned subsidiary Canyon Fuel Co. to closely held Louisville, Ky., mine operator Bowie Resources LLC for \$435 million in cash. Company CEO Eaves was quoted as saying "[t]his sale pulls forward multiple years' worth of expected cash flows for Arch, reduces our future capital outlays and further

increases our liquidity, all of which greatly enhance our financial flexibility. Moreover, Arch's ample cash balance positions the company for future debt reduction as coal markets improve."

153. As for the sale of Canyon Fuel Co., Brean Capital LLC analyst Lucas Pipes called the deal "a bit of a double-edged sword for Arch. While enhancing liquidity in this environment is a welcome reprieve, the company will be forgoing roughly one-fifth of its current EBITDA, according to our estimates," he wrote in a June 28 note.

154. On July 2, 2013, Arch disclosed that it planned to refurbish its longwall system at its Leer mine in West Virginia by the end of the year.

155. On July 4, 2013, *SNL Daily Coal Report* reported in an article entitled "Standard & Poor's reduces rating on Arch Coal senior bank debt to BB-" that

Standard & Poor's Ratings Service on July 2 reduced the issue-level rating on Arch Coal Inc.'s senior secured bank debt to BB- from BB following the company's announcement that it planned to sell several Utah coal mines.

S&P also reduced its expectations of recovery in the event of a payment default on the debt. "Our reassessment of the recovery rating stems from the proposed sale of the Canyon Fuel Co. LLC assets, which generate about \$90 million of annual EBITDA on 9.3 million tons of sales," it said.

On June 28, Arch announced plans to sell Canyon Fuel's Sufco and Skyline longwall mines and its Dugout Canyon continuous miner operation, all located in Utah, to Bowie Resources LLC for \$435 million in cash, which will boost Arch's liquidity and enhance its financial flexibility in the face of a protracted downturn in global coal markets.

S&P said the company's B+ corporate credit rating and negative outlook reflect its position as the second-largest U.S. coal producer but also its high leverage, the weak market conditions for both metallurgical and steam coal, and the company's weak credit measures.

The rating agency said Arch's debt to EBITDA ratio is expected to grow to about 10-to-1 by year-end.

156. On July 4, 2013, *SNL Daily Coal Report* reported in an article entitled “Coal producer balance sheets under pressure as market continues to flounder” that

The most heavily leveraged U.S. coal producers have been positioning themselves to withstand the protracted downturn in global coal markets by extending debt maturities, loosening borrowing terms, selling noncore assets and shutting high-cost mines to conserve cash.

But with *no end of the market weakness in sight* and the Obama administration eyeing carbon regulations that could severely hamper U.S. coal-fired generation, some analysts suggest that producers are under *even more pressure to shore up their balance sheets*.

Since the market downturn began in late 2011 to early 2012, publicly traded coal producers have pushed back billions of dollars in debt maturities to gain much needed financial flexibility. The extensions have given companies breathing room for 2013-2014, but they will start being squeezed again in 2015 and beyond when large amounts of debt begin to come due, according to an SNL Energy analysis of corporate debt in the coal sector. (Note: Debt maturing in 2013 belongs to Patriot Coal Corp., which is restructuring in bankruptcy court.)

Without significant recovery in the markets, 2015 could approach much quicker than many companies would like.

“I don’t know that the markets are going to come back by 2015,” Moody’s analyst Anna Zubets-Anderson told SNL Energy recently. She said there were few if any positive catalysts on the horizon and that sentiment in the industry was extremely low following Obama’s pledge to limit carbon emissions from new and existing coal-burning power plants.

* * *

Among the most heavily indebted coal producers are Arch Coal Inc., Walter Energy Inc. and Alpha Natural Resources Inc., all of which have suffered from declining metallurgical coal prices.

Arch, with \$5.08 billion in long-term debt, refinanced more than \$1 billion in debt in 2012, extending debt maturities and enhancing liquidity. The company also was able to get lenders to relax or eliminate financial maintenance covenants, giving it more financial flexibility. Arch has no major debt maturities until 2016. The

company recently announced the sale of its Utah coal operations for \$435 million in cash because it said the operations would have required a significant capital investment.

* * *

Analysts say that for global met coal markets to recover, significant additional production cuts are needed, particularly from U.S. producers.

157. On July 25, 2013, Arch declared a quarterly dividend of \$0.03 per share, payable on September 13, 2013, to stockholders of record on August 30th.

158. On July 29, 2013, *The Wall Street Journal* reported in an article entitled “Arch Coal Investors Lack Price Support; Investors May Be Rewarded as Gas Prices Normalize, but Tuesday’s Earnings Likely Won’t Prove a Catalyst” that

Shareholders of Arch Coal Inc. have learned to be stoic over the past five years.

Arch, the No. 2 U.S. coal producer after Peabody Energy Corp., has seen its market value slump to well under \$1 billion recently from more than \$10 billion. Its stock has lagged behind the S&P 500 by 63 percentage points this year alone.

And expectations have been dropping for second-quarter results, due Tuesday. Analysts now see an adjusted per-share loss of 34 cents, compared with a loss of 10 cents in the year-earlier period.

Arch hasn’t managed a quarterly profit since late 2011, and expectations for breaking even in 2014 have faded recently to a loss of nearly a dollar a share, according to FactSet.

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It may take a while to dig out of this hole.

159. On July 30, 2013, Arch reported its second quarter 2013 loss, again quoting CEO Eaves as saying that it “will continue to focus on the things we can control during the downturn, while carefully positioning ourselves for the market rebound. We have significantly curtailed capital spending, diligently reduced costs and further streamlined our diversified asset portfolio.

Moreover, since the market downturn began in late 2011, we have significantly increased our overall liquidity, with an ample cash position to use for future debt reduction as coal markets improve.”

160. On Arch’s quarterly results, *The State Journal* (Frankfort, KY) reported on August 2, 2013, that

Arch Coal’s CEO promises “aggressive cost reductions across all of our operations during the second half of the year” following the July 30 earnings release that showed a \$72.2 million net loss in the second quarter.

Excluding non-cash accretion of acquired coal supply agreements and asset impairment costs, Arch’s second quarter 2013 adjusted net loss was \$60.5 million.

It was the third consecutive quarterly adjusted net loss for Arch, and the fifth quarter in the past six.

161. On August 5, 2013, Moody’s placed \$5 billion of Arch’s debt on review for a possible downgrade because of continuing weakness in the coal industry. Moody’s said that if met coal prices persist at the recent benchmark settlement of \$145/tonne, Arch could be forced to make additional production cuts, leading to further deterioration in performance in 2014. According to Moody’s, “persistent negative free cash flows and tightening headroom under covenants could cause substantial erosion in the liquidity cushion in 2014.”

162. A September 20, 2013 article entitled “Coal: Bad, but Maybe Not Getting Worse” published by *24/7 Wall St.* concluded that

The coal miners already have done about all they can do to shore up their businesses. They have lengthened debt maturities, slashed discretionary capital spending, reduced marginal production and lowered costs. Now all they need is some help on pricing, but the cavalry has not arrived in force yet. Whether it arrives in time remains to be seen.

163. At a Barclays CEO Energy-Power Conference in September 2013, Arch CEO Eaves stated that the Company has a “laser focus” on production costs and is prepared to quickly respond to improvements in domestic or global coal markets with ramped-up production at little to no capital cost, and that Arch is ready to adjust but only after a “meaningful and sustainable improvement in the market.” At that point, Eaves said Arch would de-lever its balance sheet and bring idled reserves back online. Eaves also said, “We’ve been through these cycles before,” and this is the third or fourth he has seen in the last 10 to 12 years.

164. As SNL Daily Coal Report reported in a September 17, 2013, article entitled “Barclays says US coal producers realistic about state of industry”

Barclays said in a Sept. 13 research note that U.S. coal management teams delivered “refreshingly realistic messages” about the state of domestic and global coal markets at the recent Barclays CEO Energy-Power Conference.

Barclays said the commentary reinforced its view that the recent recovery in the global metallurgical coal and U.S. thermal coal markets will fall short of where it needs to be in order to justify the recent bounce in coal stocks.

“While underlying fundamentals have improved in recent months (exception being seaborne thermal [coal]), the producers highlighted the risks of idled capacity restarts, new supplies, and/or demand challenges, each suggesting coal prices will remain range bound at relatively low levels in our view,” Barclays said in the note.

Barclays said it does not expect U.S. thermal coal price recovery until possibly 2015. Barclays said Powder River Basin-exposed producers continue to lock up 2014 volumes in the “mid-\$11’s/ton,” or only marginally above cash costs of between \$10/ton and \$11/ton. Cloud Peak Energy Inc. President and CEO Colin Marshall said in his presentation that the fear of not contracting coal is worse than selling coal at current depressed prices.

* * *

“For [Arch], in our view, the management team is clearly in ‘hunker-down’ mode, and continues to manage the existing operations extremely well,” Barclays said in the note. “However, as we have flagged previously, the significant changes in [Arch]’s capital structure in the past 2 1/2 years (net debt increasing from \$1.5 [billion] to ~\$4.0 [billion] and share count increasing ~30% since Q1’11) has raised the bar in terms of the underlying long-term/sustainable coal prices needed to generate sufficient EBITDA to fundamentally justify buying the shares on typical ‘normalized’ valuation metrics.”

165. On September 20, 2013, Arch issued a statement in response to the U.S. Environmental Protection Agency’s (“EPA”) proposed New Source Performance Standards (NSPS) announced the same day, stating, in part that “The Administration’s proposal goes way too far, way too fast - and threatens to arrest rather than spur technology advances. With the world’s fastest growing economies continuing to build their economies on coal, it makes no sense for the United States - which possesses the world’s largest coal reserves - to erect barrier after barrier to coal use. In doing so, we are ensuring America higher power prices, lower economic growth and reduced international competitiveness - and effectively foreclosing on our ability to use this affordable, secure and reliable fuel in the future.”

166. On September 25, 2013, BB&T analyst Mark Levin said he expects Arch to announce additional coal production cuts from operations in Central Appalachia due to estimates that it has about 4.5 million tons unpriced and uncommitted for 2014. Levin further noted in a Sept. 24 research note that “[e]ven a big winter likely won’t save a lot of these uncommitted/unpriced tons[.]”

167. Goldman downgraded Arch to “sell” on September 27, 2013, with a price target of \$3. The analysts wrote, “[w]e assume coverage of [Arch] at Sell, with a 6-month price target of \$3, implying a -33% return vs. 7% for our coverage group. We are downgrading to Sell from Neutral given: (1) among the highest leverage ratios and lowest returns under our coverage, (2)

valuations near historical peak levels, (3) a thermal outlook less bullish than consensus, as coal plant retirements and relatively low PRB pricing will likely weigh on earnings and (4) below-average earnings growth, even if met coal prices recover above our forecasts.”

168. On October 7, 2013, Moody’s downgraded Arch’s corporate family rating to B3 from B2 and gave it a negative outlook. Moody’s estimated Arch needed significant pricing recovery in Appalachia and the Powder River Basin for its metrics to “return to sustainable levels” and said it believes thermal price recovery in Central Appalachia “is unlikely, as the region is in secular decline due to high cost of production, competition from low cost natural gas and regulations-driven coal plant retirements.” Moody’s also predicted “that continuing weakness in the global steel industry and weak Australian dollar will prevent a robust recovery in the metallurgical coal prices. The downgrade reflects our expectation that absent material upward momentum to commodity prices, Arch will continue to burn cash, and the company’s leverage metrics will remain [high].” Moody’s also said that the recent sale of Arch’s Canyon Fuels subsidiary would provide much-needed liquidity, but it saw availability of external liquidity sources as limited, given that the company’s unused \$350 million revolver contains a minimum liquidity covenant of \$450 million.

169. On October 16, 2013, *St. Louis Business Journal* reported in an article entitled “Arch Coal bonds tumble” that

Arch Coal has been hit by plunging coal prices, and the company’s bonds are now approaching levels considered distressed.

The St. Louis-based company’s \$435 million sale of three mines in Utah to Bowie Resources failed to convince investors that the move is enough to overcome a drop in earnings, Bloomberg reports.

The interest spread that creditors want to hold Arch’s \$3.5 billion of bonds instead of government debt with similar maturity has widened 108 basis points, to 993 basis points, since the asset sale

was announced in June, the news agency reports. Meanwhile among coal industry peers, there has been a contraction of 49 basis points, Bloomberg reports, citing its own data compilation.

Arch Coal is expected to post losses of more than \$1 billion from 2012 through 2014, analysts surveyed by Bloomberg said. On Oct. 7, Moody's Investors Service cut the ratings on Arch Coal's debt to B3, six levels below investment grade.

Evan Mann, an analyst with bond research firm Gimme Credit, has an underperform rating on the debt. The coal producer *is "the most vulnerable and the one who is going to get into trouble first if the market doesn't turn around,"* he told the news agency.

According to Mann, Arch has increased liquidity and argues they it will delever when conditions improve, Bloomberg reports. *"Some people in the market are not so sure that is going to happen and a restructuring may have to take place," he said.*

170. Also on October 16, 2013, *Dow Jones News Service* reported in an article entitled "Arch Coal Falls 5% as Morgan Stanley Downgrades on Cheaper Coal -- Barron's Blog" that Morgan Stanley wrote:

We are downgrading Arch to Underweight from Equal-weight, driven by our more negative view of the domestic thermal coal market. Arch is a thermal-heavy name with significant balance sheet leverage, making the company vulnerable to prolonged depressed market conditions.

171. Additionally, on October 16, 2013, *The Deal Pipeline* reported in an article entitled "Debt-heavy Arch Coal has a liquidity cushion" that

Arch Coal Inc. is saddled with heavy debt amid a troubled coal market, but a source believes the second-largest coal producer in the U.S. has adequate liquidity for at least the next 18 months.

The St. Louis-based coal producer, whose production consists of low-sulfur thermal coal from its Power River Basin mines in Wyoming and thermal and metallurgical coal from Appalachia, is *seeing its bonds trade at semi-distressed levels.*

* * *

Arch Coal is currently trying to stay liquid until coal prices rally, but the company is facing some headwinds in the near term, the source said.

“There is a lot of pressure on the coal industry domestically because coal is not the cleanest fuel and there is pressure domestically not to build any coal-fired plants because President Obama doesn’t like coal,” the source noted.

While the coal market is shrinking domestically, demand for coal is also slowing in China, which historically was one of the biggest sources of demand growth and was building a lot of coal-fired plants, the source said.

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The sale of Canyon Fuel includes the Sufco and Skyline longwall mines, and Dugout Canyon, a mechanized continuous mining operation, as well as related support facilities. All are located in central Utah.

According to the source, Arch Coal sold the properties at less than five times cash flow.

“The problem is that if you start selling assets at less than five times cash flow and your debt-to-Ebitda is 12 or 13 times, it implies that you don’t have adequate asset coverage for your bonds,” the source said.

Another problem is that, “given how lousy the coal market is, every coal company has assets to sell, but who is the buyer?” the source said.

172. On October 24, 2013, Arch’s Board declared a quarterly dividend of \$.03, payable Dec. 13, 2013 to shareholders of record on Nov. 29, 2013.

173. On October 29, 2013, Arch reported its Q3’2013 loss. Reporting on Arch’s loss, *The Associated Press* noted:

Coal producer Arch Coal Inc. on Tuesday posted a lower-than-expected loss of \$128.4 million in the third quarter as reduced expenses helped temper weaker coal prices.

* * *

Given the prolonged soft market dating to late 2011, Arch has jettisoned what it called non-core assets involving coal used by power plants to generate electricity. In August, the company completed the sale of its Canyon Fuel Co., including two longwall mines and some 105 million tons of bituminous coal reserves in Utah, to Bowie Resources, pocketing \$423 million in net proceeds.

Arch expects that deal to save it more than \$200 million in capital and administrative costs from next year through 2017, responding to what Arch CEO John Eaves called “challenging global coal markets.” The company insisted Tuesday those markets are poised to rebound at least when it comes to electricity generation, noting that coal stockpiles at U.S. utilities have dropped by more than 25 million tons since the beginning of the year.

Still, Arch said, markets for coal used to make steel remain weak, given the global glut of that type of coal and soft steel demand in Europe.

Arch said it expects 2013 sales of coal used for electricity generation to be 134 million to 137 million tons, raising the lower end of that forecast by four million tons. But Arch eased its outlook for shipments of steelmaking coal to a range between 6.9 million to 7.3 million tons, from its earlier guidance of 7.7 million to 8.3 million tons.

Arch Coal shares fell 12 cents, or 3 percent, to \$4.04 in afternoon trading.

174. An *SNL Daily Coal Report* article of November 19, 2013, entitled “Coal companies fall out of favor with largest hedge funds in Q3’13” reported that

Hedge funds sold significant stakes in several North American coal companies in the third quarter, including Alabama-based metallurgical coal producer Walter Energy Inc. and Arch Coal Inc., the country’s second-largest coal producer, regulatory filings show.

An SNL Energy analysis of quarterly Form 13F filings by seven prominent hedge funds showed that the funds collectively reduced their equity holdings of 12 publicly traded U.S. coal producers by 39% in the quarter. The analysis did not factor in options held by the funds, which are frequently used in their trading strategies. The funds’ holdings also may have changed significantly since the end of the third quarter.

175. A November 26, 2013 *TheStreet.com* article entitled “Arch Coal Needs a Spark” reported that

“Timing the bottom” of an already depressed stock is virtually impossible, especially when bearish momentum has taken hold. And if that stock happens to be in a high-risk commodity business like Arch Coal, which has always been perceived as “having potential,” investors will learn fast that things can always get worse.

Second only to Peabody Energy in terms of U.S. coal production, Arch Coal, whose stock has lost 90% of its value during the past five years, has had a hard time overcoming the misery brought upon by weak prices of coal and natural gas. Despite starting 2013 at \$7.19 per share, already 80% below its 2011 high, Arch Coal stock has lost another 40% year to date.

Even so, that hasn’t been enough to stop investors from insisting “the Street has gotten it wrong” and that Arch Coal stock has finally bottomed. While I’m willing to concede that Arch Coal’s valuation is as attractive as that of Alpha Natural Resources, which I happen to like, I didn’t come away thinking, however, that there was true long-term potential in Arch Coal’s stock following its third-quarter earnings results.

* * *

Investors will read this and accuse me of focusing too narrowly on setbacks. But given the deficits with which management has had to work -- many self-inflicted -- I’m not yet ready to give Arch Coal the benefit of the doubt. Let’s not forget that this is the same management that bet incorrectly on a transformational met coal, burdening itself with significant debt after the industry flamed out, leaving only ashes.

And it doesn’t seem as if management has gotten over that poor decision. In fairness, Arch Coal isn’t the only one that got burned. Peabody absorbed debt with its 2011 purchase of Macarthur. Alpha Natural Resources over-leveraged with its \$7.1 billion deal in 2011 for Massey Energy. The difference, however, is that those deals have not impacted how Alpha Natural and Peabody project for the future.

I won’t say Arch Coal management is scared. But I believe they’ve lost a bit of confidence following an embarrassing deal. Although there is clearly an uptick in coal demand, spurring positive

outlooks from Cloud Peak, Alpha Natural, and Peabody, Arch Coal's management does not share in the enthusiasm, stating: "So while we are seeing some signs that coal markets are poised to improve, we aren't ready to predict that turnaround will occur."

I realize my interpretation here is highly subjective. What I do know is that in an industry that has had its lunch money stolen for years, confidence matters. And while it's possible that Arch Coal is just being cautious with its guidance, I don't believe it serves their interest at this point. Nor does it help investors eager to believe in management's ability to deliver.

176. On December 3, 2013, S&P lowered Arch's corporate credit rating to 'B' from 'B+', its senior secured issue-level rating to 'B+' from 'BB-' and the senior unsecured rating to 'CCC+' from 'B-'. S&P said "Thermal and metallurgical coal markets continue to be weak, and in our view, it is increasingly unlikely that [Arch] will achieve our previously estimated sales and EBITDA targets in 2014 and 2015. As a result, we expect that credit measures will be very weak for the next couple of years." It further stated that "[i]n order to extend debt maturities, enhance liquidity, and maintain financial flexibility, the company is tendering for its \$600 million senior notes due 2016, amending its covenants, and partially funding the tender through an add-on of \$300 million to its existing term loan B." S&P concluded that "[a]lthough unlikely in the near term, we would consider a higher rating if coal demand improves and it becomes clearer that the negative trend in key credit measures will reverse, leading to leverage below 5x EBITDA."

177. On December 3, 2013, Fitch assigned a 'BB-/RR1' rating, with a negative outlook, to Arch's prospective \$300 million incremental senior secured term loans. Days after, on December 9, 2013, Fitch downgraded Arch's senior unsecured notes to 'CCC+/RR5'.

178. On December 11, 2013, Moody's said that although the US coal industry's 2014 earnings are expected to decline modestly as more lucrative contracts roll off and metallurgical coal prices remain low, the outlook for producers remains stable.

179. A December 13, 2013 article entitled “Backs against the wall, US coal producers successfully cut costs in 2013” in *SNL Daily Coal Report* reported that:

Battered for years by escalating production costs and heightened regulatory measures, several U.S. coal producers reversed the trend in 2013 in an effort to stay afloat amid industry uncertainty, according to a cost-of-coal-sales-per-ton analysis by SNL Energy.

* * *

Arch Coal Inc., which saw cost of coal sales per ton jump nearly 50% between 2009 and 2012, led major coal companies evaluated by SNL Energy with a 20% reduction through the first three quarters of 2013. One of the most aggressive producers in terms of shuttering production, Arch has reduced costs by reassessing diesel and explosives costs and techniques, eliminating contractors, shortening shifts and realigning its organization.

* * *

As evidenced by the controversial veto of a water permit for Arch’s Spruce No. 1 strip mine in West Virginia, no permit is guaranteed for coal companies. Arch has asked the U.S. Supreme Court to examine whether the U.S. EPA acted within its authority when it vetoed an approved permit for the mine.

In Central Appalachia, coal seams are thinner and more difficult to reach following decades of underground mining, hindering profitability among coal companies with assets in the basin. And in the PRB, strip ratios, which measure the volume of rock both above and within coal seams, continue to increase.

Some of the cost-cutting solutions that triggered the drop in cost of coal sales in 2013, the analysts said, are not necessarily long-term answers. Moving away from contracted labor, altering mining plans and mining specific areas to avoid paying royalties can only impact costs for so long, they said.

“I think it’s a misperception to believe the cost of mining coal has gone down,” Moody’s analyst Ben Nelson said. “In many cases, the low-hanging fruit has been cut.”

At some point, the analysts said, companies will need to restart idled equipment to meet the slight demand increase expected in 2014, partially muting the impact of selling more tons.

* * *

Buoyed by a low-cost structure, the surviving mines will likely continue to produce tons, potentially hindering price increases. It's a double-edged sword for producers - cutting costs by improving productivity can lead to oversupplied markets and weaker prices.

In 2014 Arch Fared No Better Than In Previous Years, and the Coal Market Showed Little, if any, Sign of Recovery as the Company Stock Price Continued to Decline and Plan Losses Continued to Mount

180. On January 21, 2014, Arch warned that it expects to post lower-than-planned shipments and production levels from some facilities, which should harm fourth-quarter results, disclosing that fourth-quarter shipment levels in the Powder River Basin declined by more than 15% from the third quarter because of rail service issues.

181. A February 3, 2014 *TheStreet.com* article entitled "Weak Production Still Hurting Arch Coal" showed the limited reasons to be optimistic about a comeback from Arch:

During the past five years investors in coal stocks have felt nothing but misery due to weak prices of coal and natural gas. But Arch Coal, second in the U.S. to Peabody Energy in terms of coal production, has taken more than its share of the punishment. The stock has lost more than 90% during that span.

That said, while I do believe Arch Coal stock has seen its worst, I didn't come away thinking that there was true long-term potential in the shares following the company's weak October quarter. In fact, since that earnings report, these shares have been down by as much as 6%, which has caused investors to wonder if Arch Coal is worthy of a "bottom trade." I don't have a problem with that.

* * *

Investors should pay attention to the extent to which Arch Coal management is able to reduce operating cost per ton. Although demand may be weak, there still can be an upside surprise if the company can maintain strong operational efficiency. That's been the only real distinguishing factor in a sector where everyone's struggling. In that regard, Alpha Natural Resources and Peabody stand out.

Along those lines, it's worth noting that Arch Coal management has yet to warm up to the idea that this industry can be re-ignited, despite constant claims from investors describing these companies

as “having potential.” Arch Coal management isn’t buying it. Not unlike Cloud Peak or Alpha Natural Resources, Arch Coal management has fought the pressure to fan the flames of optimism.

For instance, upon releasing third-quarter results in October, Arch Coal’s management stated: “So while we are seeing some signs that coal markets are poised to improve, we aren’t ready to predict that turnaround will occur.” While I never had a problem with this statement, it went directly against the positive outlooks issued by Cloud Peak, Alpha Natural and Peabody.

There may be some truth in what management has said. It’s also possible that they are just being overly cautious. But I wouldn’t go out of my way trying to read between any lines. This sector, particularly this company, has yet to earn the full benefit of the doubt. With debt still being a burden, I’m going to remain on the sidelines until Arch Coal can get back to posing break-even results.

182. On February 4, 2014, Arch reported an adjusted loss of 45 cents a share, which surpassed analysts’ expectations of 39 cents a share. Shares were up on the news. Earnings highlights from analysis on *TheStreet.com*’s ratings team were:

- * The company, on the basis of change in net income from the same quarter one year ago, has significantly underperformed when compared to that of the S&P 500 and the Oil, Gas & Consumable Fuels industry. The net income has significantly decreased by 380.6% when compared to the same quarter one year ago, falling from \$45.75 million to -\$128.36 million.

- * Return on equity has greatly decreased when compared to its ROE from the same quarter one year prior. This is a signal of major weakness within the corporation. Compared to other companies in the Oil, Gas & Consumable Fuels industry and the overall market, ARCH COAL INC’s return on equity significantly trails that of both the industry average and the S&P 500.

- * The gross profit margin for ARCH COAL INC is currently extremely low, coming in at 12.96%. It has decreased from the same quarter the previous year. Along with this, the net profit margin of -16.22% is significantly below that of the industry average.

- * Net operating cash flow has decreased to \$134.55 million or 48.46% when compared to the same quarter last year. In

conjunction, when comparing current results to the industry average, ARCH COAL INC has marginally lower results.

* Currently the debt-to-equity ratio of 1.97 is quite high overall and when compared to the industry average, suggesting that the current management of debt levels should be re-evaluated. Despite the company's weak debt-to-equity ratio, the company has managed to keep a very strong quick ratio of 2.75, which shows the ability to cover short-term cash needs.

183. On February 5, 2014, Arch's shares traded down 7.3% to \$3.90. *Midnight Trade Live Briefs* reported that analysts at Nomura Securities have reiterated their Neutral rating on Arch, lowering their target price on the stock to \$3 from \$4 a share, and stating "We believe that 2014 will continue to be a challenging year for Arch as weaker-than-forecast met volumes and ASPs coupled with cost pressures in the PRB result in greater FCF burn than previously modeled[.]"

184. A February 6, 2014 article in *AllAboutAlpha.com* entitled "Coal Industry in Structural Decline" concluded

what if the coal industry's struggles are not cyclical, but structural? The spike in natural gas prices may be an aberration. More importantly, forthcoming regulations on toxic mercury from the Environmental Protection Agency will put dozens of coal plants out of business. The much more significant limits on greenhouse gases from existing power plants may eliminate many more. Even if Congress or a new administration delays or prevents some of these regulations, at a minimum it is unlikely that utilities and investors will finance the construction of any new coal-fired power plants in the foreseeable future. ***This points to a structural decline, not a cyclical one.***

185. A February 6, 2014, *Barron's* article entitled "6 Beaten-Down Stocks: Values or Value Traps?" included the following:

Value Trap: Arch Coal

Arch Coal (ACI), down 35%, has been clobbered by a shift among power companies from burning thermal coal for electricity to burning cheap natural gas. A cold, snowy winter recently pushed

natural gas prices to a four-year high, raising hopes for a recovery in coal demand this year. Even a small lift would help; Arch notes that coal stockpiles for U.S. generators are the lowest since 2006.

But the case for Arch's turnaround potential would be more compelling if the company had spent the downturn cautiously scooping up assets at battered prices. Instead, it blew out its balance sheet on a 2011 purchase of International Coal Group for \$3.4 billion, just before coal prices plunged. Arch won't have to contend with debt maturities until 2018, but *[it's] extremely high leverage suggests the potential for either a big gain or a wipeout. Pass.*

186. On February 10, 2014, Arch declared an annual cash dividend of \$0.01 per share is payable on March 14, 2014 to shareholders of record on Feb. 28, 2014.

187. A February 20, 2014 *Trading NRG* article entitled "Will These Coal Companies Recover?" concluded, as a "bottom line" that

The coal industry is projected to rally in 2014, which will benefit several coal companies. The recent colder than normal weather in the U.S. pressured up the price of natural gas, which, in turn, might have also positively affect the price of coal in the first quarter of 2014. Despite the potential rise in demand for coal, its price is still expected to fall in 2014. Peabody Energy and Arch Coal continue to face narrower profit margins and tougher competition. Therefore, while coal might still offer some viable investments opportunities in 2014, Peabody Energy and Arch Coal might not offer enough to make them an investment worth considering.

188. In its March 2014 issue, *Coal Age* reported in an article entitled "Arch sells Hazard division to Blackhawk" that

Hot on the heels of its sale of the Addcar subsidiary (see Suppliers News, p. 48), St. Louis-based producer Arch Coal confirmed March 5 that it has sold its Hazard subsidiary to Kentucky operator Blackhawk Mining in a \$26.3 million cash deal. The sale includes the Hazard thermal coal mining complex and related infrastructure as well as approximately 38 million tons of thermal coal reserves in eastern Kentucky.

* * *

“The sale of our Hazard subsidiary demonstrates that we are continuing to streamline our mining portfolio and monetize assets that are not essential to our future growth plans,” President and CEO John W. Eaves said. “This transaction allows us to further sharpen our focus on strategic assets that have the highest return potential, such as our growing Appalachian metallurgical coal franchise and our low-cost Western thermal coal platform. At the same time, the proceeds from the sale further strengthen our already substantial cash and liquidity position.”

In 2013, Hazard sold 1.7 million tons of thermal coal and generated \$4.8 million in earnings before interest, taxes, depreciation and amortization.

189. On March 7, 2014, Goldman reduced its outlook for met coal pricing oversupply concerns and rated Arch Stock “sell” because of high leverage and low met coal expectations.

190. On March 17, 2014, Barclays forecasted a dismal long-term outlook for coal producers driven by weakening exports and “significant longer-term headwinds [], including ample idled production capacity available to restart if/when prices do improve, declining thermal coal exports, as well as pending new coal-fired regulations which in turn suggest the potential for *continued secular declines in US coal demand remains the most likely scenario.*”

191. A March 20, 2014 article in *24/7 Wall St.* entitled “Merrill Lynch Gets Nasty Toward Coal Stocks” reported that:

Coal may have gotten some life after the price of natural gas surged in the cold winter months. Unfortunately, not everyone thinks that the coal sector’s long-term prospects are rising. Merrill Lynch has lowered its price targets and earnings estimates on many coal sector players as the falling marginal costs will depress coal prices.

The Merrill Lynch report slashed some price targets on key coal stocks to the point that one *Underperform rating sounded like a ‘Screaming Sell’ rating.* The firm said that *met coal has defied conventional wisdom, with prices sinking through marginal costs of production and struggling to find a floor.*

Its lower estimates reflect falling costs and a view that miners will continue to resist cutting output, and an expectation of depressed fundamentals over the next several years. The firm said:

The industry can continue to be characterized by oversupply, falling marginal costs, growing substitutes, and a reluctance among miners to shut capacity given high barriers to exit. Our new 2014E benchmark hard coking coal (HCC) price forecast falls to \$132/mt from \$153 and 2015E to \$145/mt from \$160, below estimated consensus of \$154/t for 2014E and \$159/t for 2015E. Absent a weather-induced shortfall or significant capacity cuts, we expect benchmark HCC to range from \$130-150/mt over the next several years based on an estimated marginal cost of production of \$140/mt.

* * *

Arch Coal Inc. (NYSE:ACI) saw its rating maintained as Underperform as well, with the price objective cut to \$2.50 from \$3.00 (versus a \$4.35 close). Its earnings estimates were lowered to -\$1.50 from -\$1.40 per share in 2014 and maintained at -\$1.50 per share in 2015. Arch Coal shares were down almost 2% at \$4.27, against a 52-week range of \$3.47 to \$5.82. . . .

192. Merrill Lynch was not alone in its recommendation, reporting on a UBS mass downgrade of the coal sector, a March 26, 2014, *Barron's Blog* article stated

We've all heard of strip mining. Well UBS stripped the majority of the coal companies it covers-- Walter Energy (WLT), Consol Energy (CNX), Peabody Energy (BTU), Arch Coal (ACI) and Alpha Natural Resources (ANR)--of their Buy ratings today.

UBS analyst Kuni Chen explains the reason for the mass downgrades:

We expect met coal fundamentals to remain challenged and see downside risk to Street met coal forecasts. In general, we see a "muddle through" scenario for the year ahead as coal companies have cut capital spending to maintenance levels and are primarily focused on preserving/enhancing liquidity...

We do not recommend investors buy met coal levered names like [Alpha Natural Resources, Arch Coal and Walter Energy] at this time. Fundamentally, we are positive on [Peabody Energy and Consol Energy] but see both as fairly valued based on our valuation metrics and commodity price deck.

193. UBS further downgraded Arch, among other coal companies, to sell on April 10, 2014. As *SNL Daily Coal Report* reported:

UBS Investment Bank downgraded Alpha Natural Resources Inc. and Walter Energy Inc. for the second time in two weeks on yet another sharp reduction in its seaborne metallurgical coal forecast.

In an April 8 note, UBS downgraded Alpha and Walter to “sell” from “neutral.” UBS also downgraded Arch Coal Inc. to “sell” from “neutral.”

Citing a more significant oversupply situation, UBS reduced its 2014 met coal price deck to \$130/tonne from \$146/tonne. UBS cut its 2015 price deck to \$130/tonne from \$150/tonne, reflecting the outlook from Xcoal Energy & Resources CEO Ernie Thrasher, who said at a recent industry conference that the market may not rebound until 2016. The second-quarter international coking coal benchmark recently settled at a \$120/tonne, down 16% from the first quarter.

UBS cited a decline in Chinese met coal imports as the driver of oversupply, despite its model assuming the U.S. will cut 9 million tonnes of production.

“The commodity team remains unconvinced that there will be enough production cuts in the US and other regions to balance the seaborne market (17 [million tonnes of] cuts will be needed),” UBS analyst Kuni Chen said. “At current prices, US met coal is uncompetitive in Asia and the tons may shift back into the Atlantic Basin. We will be watching carefully for evidence of production cuts in the US before considering getting more constructive on met coal prices.”

UBS cut Walter’s price target to \$5 per share from \$8. UBS cut both Alpha and Arch’s price targets to \$3 per share from \$5.

“Arch has adequate liquidity to finance its cash burn and we expect management to take action to idle high-cost mines and conserve cash,” Chen said. “With \$1.2 [billion] of cash on its balance sheet and no maturities until 2018, [Arch] has more financial flexibility compared to its peers.”

194. As *Dow Jones Institutional News* reported in an April 22, 2014 article entitled “Arch Coal Loss Widens on Weaker Margins”, Arch said on April 22 that “its first-quarter loss

widened on weaker margins amid continued weakness in markets for coal used in steelmaking.” Arch reported a loss of \$124.1 million, or 59 cents a share, compared with a year-earlier loss of \$70 million, or 33 cents a share. Excluding one-time items such as prior-year acquired coal-supply impacts, the adjusted loss was 60 cents, compared with a year-earlier adjusted loss of 34 cents. Revenue decreased 0.2% to \$736 million. Company shares fell 7.8% to \$4.59 at 11:39 a.m., on the Company’s results. *TheStreet.com*, on why Arch’s stock price fell on the same day, also noted that Arch had “trimmed its shipment outlook for 2014 and now expects to ship between 6.3 million and 7.3 million tons of metallurgical coal in 2014, down from its prior estimate of 7.5 million to 8.5 million tons. Reduced met coal prices, greater supply and weaker steel demand have pressured Arch Coal and other coal producers.” The *Charleston Daily Mail* (West Virginia) reported in an article entitled “Arch Coal slashes coal sales outlook” that

While saying markets for “thermal coal used by power plants appear to be strengthening, John Eaves, Arch’s president and chief executive, said steelmakers’ demand for coal remains “soft, prompting the company’s lowering by about one million tons its sales outlook for such so-called metallurgical coal.

Arch now forecasts shipping 6.3 million to 7.3 million tons of metallurgical coal this year, down from its February outlook of 7.5 million to 8.5 million tons. The company lowered by 2 million tons the upper end of its previous guidance on sales this year of thermal coal, saying it now expects to sell 124 million to 132 million of that type of coal.

“As expected, our first-quarter results reflect a challenging global metallurgical coal market and the impact of rail performance issues, Eaves said. “At Arch, we are taking proactive steps to manage our controllable costs and capital spending, reduce our cash outflows and preserve our liquidity.

St. Louis-based Arch, among the world’s biggest coal producers, said it lost \$124.1 million, or 59 cents per share, in the first three months of the year. That’s up from a loss of \$70.5 million, or 33 cents per share, during last year’s January-through-March period.

The company's revenue slipped to \$736 million, slightly below \$737.3 million a year ago.

Analysts polled by FactSet expected a loss of 43 cents per share on revenue of \$711.4 million.

Shares of Arch Coal tumbled 42 cents, or 8.6 percent, to \$4.55 in afternoon trading Tuesday.

Intent on streamlining, Arch earlier this year sold what it called "non-strategic assets in Appalachia, including a Kentucky operation that produced coal used for creating electricity.

195. On April 24, 2014, *SNL Daily Coal Report* reported in an article entitled "US coal exports nudge higher in February, but does a weak summer loom?" that

The U.S. exported just less than 8 million tonnes of coal in February, according to U.S. Census Bureau data analyzed by SNL Energy, up 1.8% from 7.8 million tonnes shipped in February 2013 as higher exports continued to surprise industry leaders.

The February export total represented a 3.2% increase over January, driven by higher metallurgical coal and bituminous coal shipments.

The U.S. exported nearly 5 million tonnes of met coal in February, up 3.4% over the year-ago period and bringing the year-to-date total to 9.6 million tonnes, just off the pace set in 2013. UBS Investment Bank analyst Kuni Chen told SNL Energy that the U.S. needs to cut about 9 million tonnes of met coal in 2014 to help rebalance a depressed global market.

* * *

U.S. coal producers are starting to take action. Arch Coal Inc. on April 22 lowered its met coal guidance for 2014, just one week after Walter Energy Inc. announced it would idle its Canadian met coal operations. Patriot Coal Corp. on April 23 said it would likely cut production at its Wells mining complex, which produces met coal.

Met coal reductions, along with anticipated strong thermal coal demand in the U.S., may make current export coal totals from the U.S. unsustainable through the summer. David Host, chairman and CEO of shipping agency T. Parker Host, said in a phone interview April 23 that April coal shipments out of Hampton Roads in

Virginia are strong, but that is likely due to rail disruptions in March pushing back shipments.

“The question is,” Host said, “what will May and June look like?”

Host is projecting 100 million tons of coal exports from the U.S. in 2014. In its “Short-Term Energy Outlook” released April 8, the U.S. Energy Information Administration projected 101 million tons of coal exports this year, which would mark the fourth consecutive year with more than 100 million tons of coal exports.

The U.S. exported roughly 3 million tonnes of thermal coal - bituminous and subbituminous - in February, down 0.8% compared to February 2013. The February total for thermal coal was 3.8% lower than the January total.

Host acknowledged that more coal this summer “may stay home” as utility stockpiles in February reached their lowest total since March 2006, according to the EIA. The benchmark price for thermal coal imported into northwest Europe, known as API2, also is weak. According to an April 17 note from Barclays, the benchmark price was \$77/tonne as of April 16, down from \$87/tonne a year ago.

In the company’s earnings call April 22, Arch Executive Vice President and COO Paul Lang said the coal producer is forecasting a larger percentage of domestic business relative to exports, which could help improve seaborne pricing in the future.

Current seaborne prices have not dampened Arch’s enthusiasm in the long-term outlook for global thermal coal due to a wealth of coal-fired generation coming online in the next three to four years, according to Arch President and CEO John Eaves. He said during the earnings call that Arch thinks exports could total in the low 100-million-ton range this year.

“Certainly, at API prices right now, the numbers don’t work when you back them out to the mine,” he said. “The prices that we see off the West Coast certainly don’t work very well right now. We do think it’s important to continue to cultivate long-term customer relationships, because we do see long-term demand being strong in the international market. We continue to do some of that. Time will tell, but I wouldn’t be surprised to see exports still top 100 million tons for the year.”

According to the data, the U.S. shipped 435,498 tonnes of met coal to the Netherlands from the Norfolk, Va., district. The U.S. also shipped 313,000 tonnes of met coal to Turkey from the Mobile,

Ala., district. The U.S. shipped 296,421 tonnes of bituminous coal to the Netherlands from the New Orleans district.

196. A *Dow Jones Institutional News* article of May 4, 2014 entitled “Arch Coal Bonds Shouldn’t Burn Investors -- Heard On The Street” reported in relevant parts that

Coal miners’ stocks are almost as unloved as the fuel they produce -- and with good reason. Better opportunities may be found by digging elsewhere in the capital structure.

Arch Coal exemplifies Big Coal’s problems. The highly priced acquisition of International Coal Group in 2011 left Arch heavily indebted just as the shale boom made natural gas a more potent competitor to thermal coal, and as China’s appetite for U.S. metallurgical coal topped out. Arch’s net debt stood at just over \$4 billion at the end of March, nearly 17 times estimates for this year’s earnings before interest, taxes, depreciation and amortization, or Ebitda.

Little wonder Arch’s stock has dropped more than 80% in three years. That may tempt bottom fishers, but its bonds may be a better bet.

Arch has \$1 billion of 7% unsecured senior notes due in 2019. These trade at about 77 cents on the dollar, according to FactSet, implying a yield-to-maturity of more than 13%. That represents a spread over comparable Treasuries of almost 12 percentage points.

At that yield, and with the word “unsecured” looming large, the big issue is whether Arch could go under. Ebitda this year is forecast at just \$240 million, not even enough to cover interest charges of roughly \$390 million.

Yet *Arch’s debt, like its stock, is an option on a recovery in coal pricing*. And Arch has bought itself time to wait for that. Having refinanced some debt in December, it now faces no maturities until 2018, when a \$1.85 billion payment comes due. Arch has liquidity of \$1.38 billion, including \$1.16 billion of cash and equivalents.

Consensus estimates imply that after interest payments and capital expenditure of about \$190 million, Arch will burn through \$340 million in 2014. At that rate, it has about four years of liquidity left.

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So why not buy the stock? The catch is that highly leveraged companies often use a run-up in the share price to issue more stock, using proceeds to reduce debt. That would be the sensible option for Arch, diluting shareholders but further underpinning the value of the 2019 bonds.

And unlike shareholders being paid a one-cent-a-year dividend, bondholders would have been receiving payments equivalent to an annual yield of 9.1% at the current price. For them, Arch doesn't need to win any popularity contests. It just needs to survive.

197. On May 8, 2014, Fitch downgraded Arch's credit rating to CCC from B- based on its view that earnings will remain weak and cash flow will be burned through 2015, given the outlook for met coal prices. At March 31, Arch's total debt was \$5.1 billion and its current debt maturities were modest. Fitch predicted the hard coking coal benchmark price will average \$135/tonne over the next 12 months, a level that puts a good portion of global met coal supply out of the money. Shares of Arch Coal Inc. shed 4.35% on light volume to finish at \$4.18 after Fitch Ratings downgraded the company.

198. Assessing the coal industry in a May 22, 2014 article entitled "Coal: To Buy or Not to Buy", *Barron's Blog* reported:

There's been a bit of bullishness creeping into the coal stocks during the last few months. Is it time for the group to rally?

During the past three months, Consol Energy (CNX) has gained 11%, Peabody Energy (BTU) has risen 3.4% and Cloud Peak Energy (CLD) has dropped just 0.8%. (Arch Coal (ACI), it should be noted, has plunged 11% during that time period.) Is this the start of a good thing?

Macquarie's Luke McFarlane and Aldo Mazzaferro see positive signs for the coal stocks:

We continue to interpret the two diverging stories in the US thermal market; with utilities and rails believing coal is still available and being delivered, while coal producers note higher demand and order books which are close to full...Coal producers in the [Powder River Basin] continue to see material year over year

demand growth, with one noting a 30% increase in PRB utility nominations through April...

McFarlane and Mazzaferro . . . give Arch Coal a Neutral rating, as they're concerned about its cash burn.

Nomura's Curt Woodworth and team have their doubts about the Powder River Basin rally:

In our view, the market has been over exuberant about the possibility of a [Powder River Basin Coal] price spike, as inventories are now simply closer to normal levels and any pockets of tightness are likely to fade by year end. As such, we believe further downside risks exist to Arch Coal and Peabody Energy.

Investors have their doubts too, by the looks of things. Shares of Peabody Energy have fallen 2.9% to \$17.53 at 2:46 p.m. today, while Arch Coal has dropped 2.1% to \$3.78, Cloud Peak Energy has declined 1.2% to \$18.22 and Consol Energy is off 0.9% at \$44.11.

199. Picking up its prior article, *Barron's Blog* reported in a May 27, 2014 article entitled "Coal: No 'Imminent Bankruptcy Risk' But UBS Discusses Anyway" that

Pick a coal stock--any coal stock--and it's likely that those shares have been pounded this year. That's made some analysts consider whether they're cheap enough to buy. UBS thinks it['s time to consider bankruptcy, even if it['s not a near-term concern.

* * *

UBS analyst Kuni Chen explains why now's a good time to start thinking about bankruptcy in the coal sector:

Since 2012, we have seen Patriot Coal and James River file for bankruptcy protection. There continues to be signs of mounting financial distress in the coal sector with some tranches of Walter paper trading at 60 cents on the dollar. Alpha and Arch paper is trading a bit better in the 70-80 range for unsecured debt. ***With yields approaching the mid-teens percentages for Arch Coal/Alpha Natural Resources paper, the bonds are edging closer to distressed levels.*** . . . While there does not appear to be any imminent bankruptcy risk, we want to discuss the potential event path to a next potential liquidity crisis looking ahead 2-3 years. Within our coverage universe, the companies with the most financial leverage include Alpha Natural, Arch Coal, and Walter Energy.

200. Discussing the same UBS report, on May 28, 2014, 24/7 Wall St. reported:

Alpha Natural Resources Inc. (NYSE:ANR) has more than \$1 billion in cash and cash equivalents on the balance sheet and does not appear to be in an imminent threat of a bankruptcy filing. With debt comprising a large part of the company's liabilities, a Chapter 11 filing may now be the best way to go in UBS's opinion. The company may consider a debt for equity type exchange, which although dilutive, could eliminate large debt service obligations. Other out-of-bankruptcy negotiations with debt holders are also a possible solution. The Thomson/First Call price target for the stock is \$5.47. The stock closed Tuesday at \$3.69 a share.

Arch Coal Inc. (NYSE:ACI) is another troubled company that also has solid cash and cash equivalents on the balance sheet. The UBS team sees the situation at Arch akin to how things stack up for Alpha Natural. With the Mercury and Air Toxics Standards set to take effect in April 2015, many companies are retiring coal-fired plants at an increasing rate. This is yet another headwind facing the industry. Investors are paid a small 1.1% dividend. The consensus price target for the stock is \$4.36. Arch Coal closed Tuesday at \$3.73.

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While aggressive traders like to jump in and out of the coal names, the bottom line is the domestic business for the sector is ugly. Exports to countries dependent on coal with fewer environmental restrictions is really the only hope for future growth. While it is rare for entire industries to become totally extinct, it has happened before. With utilities in the United States going to natural gas and solar, it could happen here at a minimum.

201. On June 3, 2014, Arch's shares, along with the rest of the coal industry, fell 4.7% to \$3.29, on news that the EPA is proposing to cut carbon emissions in the country 30% by 2030.

202. On June 9, 2014, the *Charleston Daily Mail* (West Virginia) reported in an article entitled "Feds say future of coal bleak" that

In the latest issue of its quarterly Econ Focus magazine, staff at the Richmond Federal Reserve analyzed the potential future of West Virginia coal.

What does that future look like? Well, to use its word: "Bleak.

“The U.S. coal industry seems to be facing unprecedented economic and regulatory challenges, including substantially lower natural gas prices, more stringent environmental standards for coal-fired power plants, and higher costs for mining methods that are common in West Virginia, contributor Karl Rhodes wrote.

203. A June 11, 2014 analysis in *Trading NRG* entitled “Will These Coal Companies Do Better in the Coming Quarters?” concluded that:

The coal market is likely to keep heating up in the coming months as production picks up. Some coal companies such as Peabody Energy will see a rise in production and may benefit from these recent developments, but other companies such as Arch Coal will not. In any case, the expected rise in production isn’t likely to pull up the price of coal. Therefore, coal companies are likely to keep showing lower earnings and little to no growth in sales.

204. A July 1, 2014 *SNL Daily Coal Report* article entitled “Even if prices remain soft, Arch Coal says it can survive next 3 years” reported that

Slashed capital expenditures, asset sales, debt refinancing and the new Leer metallurgical coal mine can help Arch Coal Inc. withstand a soft market for three additional years, company management told Cowen & Co. LLC.

In a June 30 note, Cowen analyst Daniel Scott said Arch COO Paul Lang highlighted the coal producer’s continued commitment to liquidity in an effort to outlast the downturn in the met coal market. Met coal producers were dealt another blow when the third-quarter international coking coal benchmark settled at \$120/tonne for the second consecutive quarter, below Wall Street expectations.

The persistent weakness could lead to another round of production cuts in the U.S. Arch, which reported a net loss of \$124.1 million in the first quarter, lowered its 2014 met coal guidance in April. Its earnings were also hurt by poor rail performance in the Powder River Basin.

“While the PRB story appears to be intact, clearly higher met coal pricing is necessary in the intermediate term in order to begin de-levering the balance sheet,” Scott said.

205. As Arch was holding out for a turn-around, on July 9, 2014 *SNL Daily Coal Report* published an article entitled “Coal equities tumble as Morgan Stanley slashes metallurgical coal outlook” which reported:

Morgan Stanley & Co. LLC lowered its forecast for metallurgical coal prices considerably to reflect a much more gradual recovery, projecting the price to remain below \$180/tonne until 2018.

In a note dated July 7, Morgan Stanley cut its projected 2015 met coal price to \$133/tonne from \$165/tonne. It lowered the 2016 price to \$160/tonne from \$180/tonne and the 2017 price to \$170/tonne from \$185/tonne. The third-quarter international coking coal benchmark recently settled at \$120/tonne for the second consecutive quarter, below Wall Street expectations. Two years ago, the benchmark price settled at \$225/tonne for the third quarter of 2012.

Morgan Stanley analyst Evan Kurtz said the main culprit for poor pricing has been weak year-to-date Chinese imports as a result of destocking along with strong export growth out of Australia. Kurtz estimated that about 40% of seaborne supply is uneconomic on a cash costs basis - excluding maintenance capital expenditures spending - while roughly 77% of U.S. export supply is loss-making.

As a result of lowering its price deck, Morgan Stanley cut the price targets for U.S. met coal producers Alpha Natural Resources Inc., Walter Energy Inc. and Arch Coal Inc. All three coal producers saw their shares tumble during trading July 8. Walter shares dropped the most significantly, falling 8.6% to close at \$5.62. Alpha shares fell 6.9% to \$3.38, and Arch fell 4.4% to \$3.25.

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Morgan Stanley lowered Alpha's price target to \$4 per share from \$5 and Arch's price target to \$2 per share from \$3. Morgan Stanley also slightly lowered the price targets for CONSOL Energy Inc. and Peabody Energy Corp. Lower Newcastle seaborne thermal coal prices prompted Morgan Stanley to slightly lower the price target for Cloud Peak Energy Inc.

206. On July 11, 2014, Bloomberg reported in an article entitled “Metallurgical Coal to Stay Cheap for Years, Moody's Says”

Additional global supply of metallurgical coal will keep the price of the steelmaking raw material close to current low levels for the next few years, Moody's Investors Service said.

Most U.S. production is unprofitable at current prices while as much as half of global output is making a loss, Anna Zubets-Anderson, a Moody's analyst in New York, said today in a statement from the ratings company.

The commodity has slumped on a slowdown in demand from China, the world's largest steelmaker, and an expansion of coal output in Australia. The market was oversupplied by about 30 million metric tons at the end of the first quarter, despite global production cuts of more than 40 million tons in the past two years, Moody's estimated today in a separate report.

The international quarterly benchmark price for metallurgical coal, also called coking coal, is at a six-year low of \$120 a ton. The current price is unsustainable and will recover to \$135 to \$145 by the end of 2015, Moody's said.

* * *

U.S. coking coal miners won't be profitable as a group until the benchmark price reaches \$160 to \$170, Moody's said. They could supply over 50 million metric tons this year while burning more than \$1 billion in cash, it said.

207. As the prior three paragraphs show, Arch could possibly hold out for 3 years, but would be unlikely to turn the corner during that time, as its met coal production would still likely be unprofitable, or barely profitable, if the estimates of Moody's and Morgan Stanley held up.

208. On July 21, 2014, Arch announced that it was idling its Cumberland River coal complex and eliminating 213 full-time jobs in response to the "currently challenged metallurgical coal markets[.]"

209. On July 28, 2014, in anticipation of its forthcoming earnings announcement, Arch's stock hit a new 1-year low, closing trading as low as \$2.82 and closing at \$2.84.

210. On July 29, 2014, Arch reported a net loss for the second quarter of 2014 of \$96.9 million, or \$0.46 per diluted share. Revenue fell 6.9% to \$713.8 million, slightly below analysts'

mean estimate of \$716 million. Chief Operating Officer Paul A. Lang said the company expects “strong cost performances in our Appalachian and Bituminous Thermal segments to continue, and we plan to remain nimble in response to market conditions.” Arch also reduced the high end of its sales volume targets for 2014, reflecting “the result of ongoing transportation bottlenecks affecting thermal coal deliveries and the impact of metallurgical production curtailments.”

211. On an earnings call discussing the results, Company CEO Eaves stated “We’re certainly disappointed in the pricing, but we don’t think this pricing is sustainable.”

212. On to Arch’s earnings, a July 29, 2014, *Platts Coal Trader International* article entitled “US miner Arch expects soft met coal prices, lower 2014 US coal exports” reported:

US miner Arch Coal said Tuesday it expects tough conditions in the met coal market for the rest of 2014, and that total industry-wide US coking coal and thermal coal exports won’t reach 100 million st, leaving shipments down by over 15% on last year.

In a quarterly earnings statement, Arch said “prevailing soft seaborne thermal and metallurgical prices” would limit overseas coal trade from the US.

* * *

Arch has 6.2 million st in 2014 met coal sales committed, with 6 million st of it priced at \$82.44/st. In 2015, committed met coal sales total 1.9 million st with 1.6 million st priced at \$85.53/st.

In Appalachia, met coal contributed a larger share to the regional sales mix over the second quarter of 2014, which totaled 3.7 million st including bituminous thermal, compared with overall sales in Q2 2013 of 4 million st. Total sales in Q1 2014 were 3.6 million st.

Arch’s Appalachian mines saw a cash margin of \$7/st in Q2, down from \$8.48/st in Q2 2013, but improved on Q1 2014’s \$2.22/st as costs improved.

Operating margins were negative at \$6.89/st in Q2, improving on Q1 2014’s \$13.1/st operating loss, and compared to a \$5.38/st operating loss in Q2 2013.

At the Leer mine producing high-vol met coal, Arch said it was successfully ramping up to full production.

“Our successful cost control efforts to date—underscored by strong operating performances at Leer in Appalachia and West Elk in Colorado—have allowed us to reduce our cost-per-ton expectations for those segments in 2014,” Eaves added.

213. Further demonstrating the troubles faced by Arch, an August 28, 2014 *SNL Daily Coal Report* article entitled “Analysts: ‘Everything is not OK’ for coal, as industry ‘just can’t catch a break’” stated in part that

New research reports out on the coal industry paint another gloomy picture of coal markets, regulations, poor rail service, natural gas competition and other obstacles, despite a recent uptick in coal equities.

Mark Levin, an analyst with BB&T Capital Markets, wrote in an Aug. 26 note that it would be “hard to argue anything has gotten better for the US coal industry in August” with the exception of equity prices. Coal equities, Levin notes, were up an average of 3% in August, on pace with a 3% rise in the S&P 500. Levin says the recent outperformance is likely due to the equities attracting the attention of “deep-value, heavily contrarian investors” and recognition among investors that many coal companies have enough liquidity to withstand poor conditions for a while.

“With only [approximately \$20 billion] of total market cap left for the entire publicly-traded US coal industry, there seems to be more momentum toward taking a flier, no matter how expensive the underlying option may be,” Levin wrote.

Jefferies LLC analyst Peter Ward reminded clients in an Aug. 27 note that the firm had urged caution on coal equities early in the year.

“Our concern was that a weather-driven rebound in gas prices above \$4 led some to believe everything was OK for coal,” he wrote. “Everything is not OK.”

* * *

“Coal companies just can’t catch a break,” Levin wrote. “While the Class I rails continue to report record earnings, coal prices, both in the east and the west, remain constrained. Granted, unusually mild spring and summer weather has played a big role by allowing

utilities to rebuild inventories, but domestic rail service woes, caused by an unusually harsh winter and a resurgence in demand across most commodity groups, continues to create headaches for coal producers.”

Because of certain challenges facing the industry, Jefferies warned investors to specifically avoid Alpha Natural Resources Inc. and *Arch Coal Inc. due to their “higher risk”* and instead selected hybrid coal and natural gas producer CONSOL Energy Inc. as its top pick.

Lucas Pipes of Brean Capital LLC published a note Aug. 27 with key takeaways from a recent visit with Arch’s management.

“Arch reiterated that it feels well positioned to weather the current market downturn with its \$1.25 billion in liquidity and no maturities coming due until 2018 (which is also first lien secured). Arch stated that it did not anticipate exchanging its \$250 million revolver (included in liquidity of \$1.25 billion) into other forms of secured debt at the moment,” Pipes wrote. “Still, the company was keen to note that it was maintaining an eye on further market conditions and its liquidity position.”

Pipes said Arch management also believes that the metallurgical coal market will stabilize and that prices have finally bottomed. He said Arch is optimistic that met coal market dynamics could shift more positively during 2015 on a combination of supply cuts and slowing capacity growth from Australia.

Levin wrote that coking coal prices “remain remarkably flat.” He said he thinks the likelihood of a met coal benchmark price settlement of \$120/tonne in the fourth quarter is increasingly likely. The benchmark price has settled at that level in both of the last two quarters. He also wrote that while there is interest in coking coal assets coming from Indian companies, they are not currently searching for assets in the United States, preferring to look to Australia instead.

“This shouldn’t come as a surprise to anyone who understands the delivered costs of coking coal, but it’s a reminder that ... the U.S. is unlikely to be a major player in helping India meet its burgeoning infrastructure needs going forward,” Levin wrote.

Ward said that while Jefferies does expect a modest recovery for seaborne met coal, it does not believe a recovery is likely to improve the competitiveness of U.S. met coal producers. Ward

added, “it is important to remember that U.S. met coal was largely uncompetitive for a very long time.”

214. During August of 2014, there was significant growth in short interest in Arch, and it was reported that approximately 19.9% of the Company’s shares are sold short.

215. On September 2, 2014, Morningstar gave Arch a “B-” rating indicating a high default risk.

216. On September 3, 2014, S&P revised Arch’s rating outlook to negative due to the gloomy outlook of the metallurgical coal market and reflecting “the potential for a downgrade if average met coal prices do not improve in line with [S&P’s] expectations of \$140 to \$160 per ton in the next 12 to 18 months,” which price situation would cause Arch to use up cash and liquidity faster than expected.

217. On September 5, 2014, *SNL Daily Coal Report* published an article entitled “Arch open to monetizing noncore assets as coal markets shift focus” which reported:

Arch Coal Inc. CEO John Eaves said the company is trying to come out stronger on the other side of a “perfect storm” of industry challenges and is open to offers on some of its assets as it increasingly focuses on metallurgical and western coal segments.

While speaking at the Barclays CEO Energy-Power Conference, Eaves declined a question about which specific assets might be considered for sale. Past Arch divestitures have included its Hazard mining complex in the Central Appalachia coal basin and its ICG ADDCAR Systems LLC subsidiary, as well as a couple of Utah longwall mines.

“Our strategy is to continue to maximize our position in the Powder River Basin, continue to build out our supply on the met side, which we’ve done, and really maximize what we’re doing in Colorado and Illinois. As long as we get that right we’ll be in good shape,” Eaves said. “We have some assets that don’t have to be a part of our long-term plan. If you look at our liquidity and where we are today, we don’t feel compelled that we have to do anything. It’s a matter of value.”

Eaves' comments suggest that Arch's focus on other regions and met coal may mean that, like other producers, it would be willing to part with some of its thermal coal operations in Appalachia. Praising the PRB's potential and noting that a project Arch is holding in the Illinois Basin could position that region as a core operating segment, Arch is primarily focused on Appalachia's met coal deposits and cutting its mining costs there.

"We think you need \$5-plus natural gas [prices] on a sustained basis for Central App to be competitive," Eaves said. "So, what you've got in Central App is a lot of thermal coming out and more of a focus on the met market."

Eaves said the company is working hard to diversify its asset base and has capacity that it can bring on in the PRB, where it operates the massive Black Thunder mine in Wyoming. He said bringing that capacity back on will not occur overnight and will require an improvement in market prices.

"That's a sustained, improved market, not just a quarter or two or year or two, but the ability to really capture a multiyear improvement in the market," Eaves said. "Currently, we don't have any plans to bring that capacity back on, but it's there. It would not take any capital expenditure and we could do it in a matter of months."

He added that even with a "tough regulatory environment," the PRB is expected to do well and that Arch "can make a lot of money" in domestic markets. Eaves said access to international markets will be Arch's primary focus for growth and that the company is currently working on several fronts to open up U.S. port capacity. He added that the growth opportunities are beyond China and India and also include Southeast Asia, South Korea and Japan.

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Eaves also said that met coal markets, increasingly a focus for Arch, have bottomed out. Many coal producers have found the current met coal international benchmark price of \$120/tonne unsustainable, but producers have been slow to rationalize production levels.

"We think that the question becomes whether we move along the bottom with current pricing or we bounce up from the bottom," Eaves said. "And as we know from history, typically when these

markets balance, they overcorrect and create real opportunities for the companies that are well-positioned to respond to those.”

218. On September 18, 2014, Goldman published a report claiming that prices for metallurgical coal have not yet hit a bottom and downloading one of Arch’s peers.

219. On September 16, 2014, analysts at Northland Securities and at Nomura downgraded Arch Stock from “neutral” to “reduce” rating, with a \$1.50 price target. Five days earlier, analysts at Citigroup had reiterated a “neutral” rating on shares with a \$3.50 price target.

220. On September 23, 2014, BB&T analyst Mark Levin reported wrote: “The reality is investors hate coal at the moment. And that isn’t likely to change given (a) the long amount of time necessary to remove the current met/steam over-supply overhang and (b) governments around the world - save India - continuing to create policies to limit the fuel’s usage.”

221. On September 25, 2014, Arch’s shares traded as low as \$2.01 and closed at \$2.14.

222. On September 26, 2014, the *St. Louis Post-Dispatch* (Missouri) reported in an article entitled “Coal companies having tough year so far” that

It was supposed to be a better year for U.S. coal producers.

But railroad congestion, a mild summer and indications that coal prices have yet to hit bottom have all conspired against the fuel, while cheap and plentiful natural gas continues to put pressure on the industry in the U.S.

U.S. coal producers have seen their share prices hit especially hard in the last several months. Though environmental rules are making new coal plants prohibitively expensive and leading to the closure of some older plants, it’s really market conditions -- oversupply and the advent of cheap natural gas -- that are hitting coal miners hardest, said Ken Colburn, a senior associate at the Regulatory Assistance Project who specializes in air regulations.

“I don’t think this is an easy cakewalk necessarily, but nothing the (Environmental Protection Agency) does will lead to the kind of impact on coal as a fuel that the market is having,”

* * *

Creve Coeur-based Arch Coal's share price is down 31 percent over the last month.

The negative sentiment also has hit the company's debt. On Thursday, the price of Arch Coal's 7 percent bonds that mature in 2019 tumbled to 53.75 cents on the dollar, its lowest price ever, according to Bloomberg News.

* * *

Australia and Indonesian coal producers will pivot to India and South Africa, and their suppliers will pivot elsewhere in the global seaborne market. That could hurt U.S. producers like Arch, which hopes to nearly triple its exports to 30 million tons by 2020, according to an investor presentation.

"Ultimately, U.S. coal, which was really a swing supplier anyway, is most likely to be forced out of the seaborne market," Inton said.

Arch, however, said most of China's coal imports already meet the quality guidelines it announced last week. Reuters reported last week that power plants may also be exempted.

"Europe and the Americas, as well as Japan and South Korea, are more natural markets for U.S. thermal coals, but actions taken by China can have impacts on the seaborne marketplace," Arch Coal spokeswoman Logan Bonacorsi said.

223. Also on September 26, 2014, *SNL Daily Coal Report* reported in an article entitled "At industry conference, mood reflects troubling coal market sentiment" that the Met coal outlook was especially bleak and that

Distress over the strengthening U.S. dollar, continued worries over China's economy and mentions of possible bankruptcies in the coal industry contributed to the sell-off in the coal sector and a gloomy mood at an industry conference this week.

It was an "awful week" for coal, one industry source said, and the conference sentiment already was reflecting the market by the time Xcoal Energy & Resources President and Chief Commercial Officer Jack Porco delivered his presentation during the afternoon of Sept. 22.

"I'll try to give a more upbeat view," Porco said at the Platts Coal Marketing Days conference in Pittsburgh. "It's going to be tough."

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“I guess if I only had any piece of advice, it’s get ready and implement a survival plan, protect and sustain your business until we get to where the market improves,” he said. “Is it 2016? Is it 2017? Is it 2018? Hopefully, it’s sooner than that. But we’re saying it’s around 2017 or 2018.”

224. On September 29, 2014, Barron’s Blog reported in part in an article entitled “Coal: When Tax Loss Selling is a ‘Better Opportunity Than Hanging On’” reported that:

As for Arch Coal and Alpha Natural resources, Bridges dubs them the “terrible twos.” He explains why:

...after falling from peaks of \$67 and \$36 respectively, both Alpha and Arch now trade with a \$2 handle. The stocks are essentially trading as options on a coal sector recovery while some of their higher risk debt is sending a message by trading between \$.60 and \$.70 on the dollar. Arch has \$4.2bn of net debt carried by \$0.47bn of market capitalization while Alpha is only half as leveraged... However, both companies have balance sheet liquidity and have pushed out debt maturities to give themselves time for the coal market to recover. The only thing missing is the catalyst....

225. On October 2, 2014, Moody’s projected at least another grim 12 to 18 months for the coal industry, with the industry being “stable but weak.” Moody’s analyst Anna Zubets-Anderson wrote that the weakest positioned coal producers are those that took on a large amount of debt at the top of the market such as Arch. She also wrote that “If you have the \$120 benchmark price that we have today persist for longer than we think, I think we’re going to have more bankruptcy,” Zubets-Anderson said in an interview. “They’re probably going to come from weaker positioned coal producers.”

226. Similarly, on October 6, 2014, Goldman analysts said they are not yet ready to call a bottom in plunging coal markets and reduced their forecast for met coal pricing. Arch shares fell 5% on the news, because it had been focused on growing its met coal portfolio.

227. On October 8, 2014, Morgan Stanley's commodity team lowered its hard coking coal price forecast to \$125/t for 2015, predicting a more gradual price recovery than had been expected. Morgan Stanley noted that the timing of a met coal price rebound is becoming increasingly important for liquidity-constrained met coal producers like Arch.

228. On October 9, 2014, the *St. Louis Post-Dispatch* (Missouri) reported in an article entitled "Daily Wrap: Bears pounce on Arch and Peabody" that

DARK DAYS FOR COAL: Bond investors have placed Arch Coal on the critical list, bidding the company's 7 percent bonds (due in 2019) down to less than 40 cents on the dollar. They traded at 70 cents a month ago. Arch shares have been hit too; they fell 7.2 percent today and are down 65 percent so far this year. A Morgan Stanley analyst said Wednesday that a recovery in the price of metallurgical coal, a key Arch product, will take longer than expected....

229. On October 13, 2014, Arch scheduled the release of its third quarter 2014 results for October 28 and disclosed the following:

Separately, in light of the recent unprecedented market conditions, Arch has elected to provide the following selected preliminary results regarding its third quarter 2014 financial performance and liquidity position.

Arch expects to record adjusted earnings before interest, taxes, depreciation, depletion and amortization ("Adjusted EBITDA") of \$70 million to \$74 million for the third quarter of 2014, representing an improvement versus the second quarter. As of Sept. 30, 2014, Arch held \$1.05 billion in cash and short-term investments compared with approximately \$990 million at June 30, 2014, reflecting an increase of nearly \$60 million. In addition, Arch's available liquidity, which includes its cash position and undrawn borrowings on its credit facilities, totaled \$1.3 billion at the end of September.

230. On October 15, 2014, BB&T analyst Mark Levin said that investment funds are buying coal bonds and shorting equities against those positions, and that "people are shooting commodity stocks first and asking questions later as sentiment has gone from abysmal to near

‘suicidal.’” He said short interest in Arch has grown from 20% to 22% since the beginning of the quarter.

231. Also on October 15, 2014, Arch was rated “underperform” by Bank of America analysts, with a \$1.00 price target on the stock, down from their previous price target of \$2.50.

232. On October 28, 2014, Arch reported a quarterly loss of \$97.2 million, \$.46/ share.

233. On October 30, 2014, Barron’s assigned an Underperform rating and a one-year price target of 75 cents to shares of Arch and a Sell rating to its term loan. Barron’s further said that Arch’s senior note maturities cannot be refinanced unless met-coal prices move back above \$170 a ton, a prospect that looks unlikely, and therefore restructuring on or before the May 16, 2018, term-loan maturity seems likely, an event that could severely impact the value of existing equity. We therefore have to estimate recoveries based on assumptions for normalized coking coal that would prevail at the time of filing. At current pricing (\$120 a ton), value stops at the first or second-lien tranches; at \$140 a ton, value could stop at the senior notes, at prices above that, the senior notes become interesting.

234. An October 31, 2014 article in the *St. Louis Post-Dispatch* (Missouri) entitled “Investors flee Arch debt, driving down its bond prices” reported that prices for most of Arch’s “unsecured corporate bonds have fallen below 50 cents on the dollar in recent weeks as concern mounts that steam coal demand and prices for metallurgical coal - coal used to make steel - won’t rise fast enough over the next few years to save the company from bankruptcy.” And that “[b]ond prices that fall that low is ‘a sure sign of death,’ Scott Colbert, head of fixed-income investing at Commerce Trust Co., said. ‘You don’t recover from that very often.’” The same article reported that St. Louis-based Stifel, in a note to investors, called Arch a “high-risk, high-reward option for investors anticipating a strong positive turn in coal markets.” The article noted

that “Arch has more than 25 times more total debt than [EBITDA]. Evan Mann, a high-yield bond analyst at corporate bond research firm Gimme Credit LLC, said in an interview that that level ‘is just not sustainable’” and “While liquidity remained steady and the free cash flow shortfall manageable due to cost control efforts and reduced capital spending, credit ratios continue to deteriorate with leverage reaching an unsustainable, nose-bleed level[.]” Mann further stated “It’s kind of getting away from [Arch.] The only Hail Mary for them is sometime next year we have a more meaningful recovery than people are expecting in coal fundamentals.”

235. A November 4, 2014, *Business Monitor International* article entitled “Coal: Long-Term Woes To Persist” reported

BMI View: US coal production will fall in the coming years, seeing average annual declines of 0.2% in 2015-2018, with total production of 899 mnt in 2018. Coal producers will come under increasing pressure due both to subdued global prices for thermal and metallurgical coal, and to a more challenging domestic regulatory environment.

* * *

Ultimately, we believe thermal coal’s share within the US power market will decrease further over the decade. Coal consumption used for electricity generation will increase slightly in volume terms, but its share of total electricity generation will continue to decline and fall to around 35% by the next decade, according to the EIA. Emissions regulations on new coal power plants, as well as new regulations on existing power plants proposed in June 2014, have made the policy environment unfavourable for future investment in coal-generated electricity. Should the EPA regulations stand up to legal challenges, more coal-fired power plants could be taken off line sooner than expected. We expect utilities and energy companies to continue switching to gas over the coming years due both to domestic production increases and federal regulations. The abundance of gas-fired power plants under construction and the shuttering of older, less efficient coal plants are indicative of the shift.

236. A November 6, 2014 report in American Banking and Market News reported that approximately 24.7% of Arch’s shares are short sold.

237. In a Nov. 17 report, BMO Capital analyst David Gagliano, formerly of Barclays, rated Arch underperform, noting that BMO maintains a view that meaningful exports of PRB coal over the next 10 years is unlikely due to permitting challenges, increased challenges facing financing capital investments needed to develop ports, and soft international pricing “which has essentially rendered PRB exports to Asia uneconomic.”

238. The *Wall Street Journal* reported on November 24, 2014, that “[h]edge funds are betting that some of the largest U.S. coal companies are heading for the financial slag heap” and that Arch had seen heavy interest from distressed-debt buyers. The article noted that “[f]ear that the cash will run out before coal prices rebound has flushed many traditional investors, like mutual funds, out of the companies’ stocks and bonds.”

239. On December 22, 2014, *Resource Investing News* reported in an article entitled “Coal Outlook 2015: Material Recovery in Pricing Still a Few Years Out” that:

To be sure, it hasn’t been the best year for coal. Both the thermal and metallurgical spaces have been plagued by oversupply and falling prices, and continued cost cutting on the production side has led to an ever-dropping floor. Both met coal and thermal coal hit multi-year lows in 2014, with prices falling to around \$120 and \$65 respectively. According to the Financial Times, met coal has lost 16 percent this year, while benchmark Australian thermal coal has fallen 25 percent. . . . Wood Mackenzie analyst Joe Aldina . . . suggested that while a material recovery in coal prices is likely still ‘a few years out,’ for the long term, well-capitalized investors who are comfortable taking some risks could find opportunities in the coal space. [footnotes omitted]

Arch Enters 2015 Facing Persistent Headwinds, with Heavy Debt, Slim Profitability, and a Declining Outlook for the U.S. Coal Market

240. On January 14, 2015, Barclays said that it saw “persistent headwinds” for coal pricing and rated Arch as “underweight” because of heavy debt and slim profitability. Barclays analyst Matthew Korn wrote that “[t]here is really not much [Arch] can do except curtail marginal mines, conserve liquidity, and hope for a price upturn.” Korn also wrote that “coal

markets have yet to fully adjust to a still declining outlook for U.S. coal burn and a China with much less robust import requirements,” and that “[o]ppportunity will come for U.S. producers in the low-cost PRB and Illinois Basin, but this will largely reflect taking greater share of a shrinking pie.” Korn said Arch is struggling with high debt loads and interest expense after acquiring International Coal, and that Arch would benefit from constructed coal terminals on the US Pacific Coast *and* steel production accelerates in China, but that neither of those event is likely to occur in the next two or three years. He warned that “if coal prices continue to drift downward with the energy complex, given the company’s debt and interest obligations” there is substantial downside risk.

241. On January 23, 2015, Arch shares fell another 9.32% after S&P issued a bearish note on coal prices based upon its “based on our assumption that coal prices will remain depressed for at least another year.”

242. A *SNL Daily Coal Report* article on January 23, 2015, entitled ““The world is swimming in cheap BTUs’: Oversupply heaps pressure on coal sector” reported that

Analysts do not believe the beleaguered U.S. coal industry will receive meaningful relief from depressed prices in 2015, making the divide between the likely survivors and higher-cost coal miners even more prominent.

* * *

Both Morgan Stanley and Cowen unveiled grim outlooks in their respective revised price forecast. Morgan Stanley’s Central Appalachia thermal coal forecast is now just \$50/ton in 2015, down from \$57/ton, and \$55/ton long term compared to \$65/ton previously. Morgan Stanley also expects Newcastle thermal coal prices to remain capped in the long term.

Cowen reduced its average 2015 premium metallurgical coal price to \$120/tonne. Cowen cut its 2016 price to \$131/tonne and introduced a 2017 price of \$140/tonne, reflecting a very gradual price response to moderate supply curtailments amid a relatively

steady demand environment. The current international benchmark price is \$117/tonne.

* * *

The outlook is less favorable for coal producers levered to met coal, such as Alpha and Arch Coal Inc. Morgan Stanley's new hard coking coal price for 2015 is \$122/tonne, down from \$125/tonne. Morgan Stanley does not foresee a medium-term increase in prices, with its 2016 forecast now \$119/tonne, down from \$160/tonne.

* * *

Arch's balance sheet remains "meaningfully stressed," Morgan Stanley said. Its price target for the company is \$1 per share.

"We expect higher cost coal miners with stressed balance sheets to continue to draw down liquidity as they face an uncertain future," Kurtz said. "Accordingly, we are Underweight Arch and Alpha. ***We expect these names to have a binary future wherein they either survive the commodity downturn or face restructuring.***"

243. On February 1, 2015, *The Financial Times* reported that Nomura analyst Curt Woodworth predicts "multiple bankruptcies in US coal over the next 12-18 months" and that "The outlook isn't good: the outlook is getting worse." The article also reported that as a result of a slowdown in China, met coal prices have slumped from \$330 in 2011 to \$117 per tonne.

244. On February 2, 2015, Moody's downgraded Arch's Corporate Family Rating (CFR) to Caa1 from B3, probability of default rating (PDR) to Caa1-PD from B3-PD, senior unsecured ratings to Caa2 from Caa1, rating on second lien notes to Caa1 from B3, and senior secured credit facility rating to B2 from B1. At the same time, Moody's lowered its Speculative Grade Liquidity (SGL) rating to SGL-3 from SGL-2, with a negative outlook. Moody's wrote:

The downgrade reflects the weak debt protection metrics and high leverage (23x as measured by the debt/EBITDA ratio for the twelve months through September 30, 2014), which we expect to continue to deteriorate given weak metallurgical coal market conditions. We believe that metallurgical coal prices are unlikely to recover within the next eighteen months to a level that would contribute to a meaningful turnaround in performance.

Consequently, leverage is anticipated to become more elevated and further strain the capital structure.

* * *

The change to a SGL-3 rating reflects expectations for the company to continue to be cash consumptive. As of September 30, 2014, Arch's liquidity position predominantly consisted of just over \$1 billion in cash and short-term investments. The company has no meaningful maturities of debt until 2018, and they have suspended or eliminated most financial maintenance covenants that pertain only to their \$250 million revolver until June of 2015, when a relaxed, senior secured leverage ratio covenant becomes effective. Until then, only a minimum liquidity covenant of \$550 million remains in place. The revolver expires in June 2016.

* * *

The negative outlook reflects our expectation that market conditions, particularly for met coal, will remain depressed into 2016 and that Arch's performance will continue to be pressured by the weak fundamentals.

245. On February 3, 2015, reported a loss of \$240.1 million, or \$1.13 per share, for the fourth quarter. Arch also announced that it will stop paying dividends to investors to preserve cash and that it had frozen its defined benefit pension plan. Arch also said that it expected the domestic market to remain challenging due to the impact of mild winter weather on coal consumption, natural gas pricing, inventories, and new regulations slated to take effect.

246. SNL Daily Coal Report on February 3, 2015, reported in part that

In a recent research note, BB&T Capital Markets analyst Mark Levin said that given equity prices and bonds of both Alpha and Arch trading at exceedingly depressed levels, "it's clear the investment community has serious doubts about both companies' ability to survive in their present form." He estimated both producers have enough cash remaining to survive two to three years.

"Ostensibly, that's plenty of time to hope something positive happens to coal prices, but it's not clear, at least to us, what that might be," Levin wrote. "Moreover, some believe the boards could

arrive at decisions before that point. Most investors to whom we speak seem to think restructurings are inevitable. Time will tell.”

247. A February 7, 2015 *24/7 Wall St.* article entitled “Can Coal Make a Comeback?” concluded that “[t]he short-term outlook for coal, both domestically and internationally, is weak. The long-term outlook could be even weaker. Coal stocks trade more than 25 million shares a day, likely on the hope that the share price will move a little one way or the other and a trader holding enough shares that went in the correct direction will have a mini-score.” Yet Defendants continued to allow the Plan to hold Arch shares for Participants’ retirement savings.

248. On February 19, 2015, *The Messenger* (Madisonville, Kentucky) reported, in an article entitled “Analysts believe 2015 poised to be coal’s worst year ever”, that James Stevenson, director of North American coal for the research organization IHS Energy, said 2015 would be the “worst year in years probably” for coal companies.

249. *Barron’s Blog* noted in a February 26, 2015 article entitled “A Bottom for Coal Stocks?” that Arch “acquired so much debt that [its] equity effectively has become primarily an ‘option’ on fluctuations in the coal market until [it] start[s] re-financing debt as its comes due.”

250. BB&T Capital Markets analyst Mark Levin noted in a March 10 report that Chinese steel prices are down 15% year to date and that the Chinese government’s efforts to curb overcapacity and pollution could pressure steel production. “[This is] not good for those hoping for a met coal recovery in 2015,” Levin wrote.

251. A March 12, 2015 *SNL Daily Coal Report* article entitled “Fundamentals could drag Q2’15 met coal benchmark lower” reported that “[s]ince the first-quarter 2015 [metallurgical coal] benchmark settled at \$117/tonne in December 2014, the Australian dollar has weakened” and that Q2’15 settlements could be slightly lower than the [Q1’15] settlement” according to BMO Capital Markets analyst Jessica Fung. BMO further noted without 20 million

tones of supply cuts, met coal prices would remain lower for a long time. In a Feb. 19 report, Stifel Nicolaus & Co. analyst Paul Forward wrote about the met coal market's impact on Walter Energy Inc.'s declining cash reserves: "On our base case estimates through 2016, Walter would exhaust its remaining cash balance by mid-2016, leaving little or no value for ... shareholders in the absence of a met coal market recovery well above our base case price forecast."

252. Also on March 12, 2015, Moody's changed its industry outlook on the North American coal sector to negative from stable, saying that persistently weak demand for metallurgical coal and natural gas prices challenging the U.S. thermal coal sector will exacerbate the industry's long-term, secular decline. Moody's noted that Arch would be among the most vulnerable coal producers going forward.

253. On March 18, 2015, *News Bites* reported that Arch's the prices on Arch's bond, which matures in 4 years and 3 months, had slid by 20% in the past two days and that its yield to maturity has increased by 223.4 basis points from 60.24% to 62.48%.

254. On March 30, 2015, *Bloomberg News* reported that Central Appalachia coal mines were operating at a loss of about \$15 on every ton of coal produced, but that Arch would have \$418 million in liabilities as of December 31, 2014, if it closed its Central Appalachia mines. For the sake of comparison, on April 15, 2015, Arch's total market capitalization was \$224.29 million. So Arch functionally had no choice but to continue producing coal at a loss.

255. On April 21, 2015, Arch reported a net loss of \$113.2 million in the first quarter of 2015. CEO John Eaves said during an earnings conference call with investors and the media that the many headwinds affecting the coal industry will continue to drive down thermal and met demand domestically and internationally, and production will be cut in response to the drop in sales.

256. John Drexler, Arch's senior vice president and CFO, repeated the Company's mantra of being: "focused on managing our available liquidity through these difficult conditions."

257. On April 24, 2015, *SNL Extra* reported in an article entitled "BB&T: Arch Coal unlikely to file for bankruptcy in 2015, but risks loom in 2016" that BB&T issued a research note predicting that Arch "will likely make it through 2015 without filing for bankruptcy, but a restructuring is 'possible in 2016' as the outlook for coal prices softens and the producer's debt continues to far outweigh earnings." The article further reported:

Arch's large cash position of \$940 million means the company "simply has no incentive" to file for bankruptcy this year, creating a "limited likelihood of a restructuring in the next six to 12 months," BB&T analyst Mark Levin said. Arch's first-quarter EBITDA of \$82 million exceeded BB&T's estimate for \$79 million, helped by lower-than-expected cash costs.

* * *

But total revenue dropped to \$677 million, below BB&T's forecast for \$727 million and year-ago results of \$736 million, as Arch's average sale price declined 4.5% on the year to \$19.18/ton on softer metallurgical and Central Appalachian thermal prices. No recovery is seen in the near term, with BB&T lowering its full-year 2015 price decks for Arch's unpriced Powder River Basin, Central Appalachian thermal and met coal sales.

The dimmer price outlook and a drop in Arch's sales volume guidance make it difficult to envision a major de-leveraging, BB&T said. The company has \$5.15 billion in total debt compared with the analyst's EBITDA forecast of \$285 million this year.

preponderance of natural gas and the strong U.S. dollar that holds back the competitiveness of U.S. exports almost assures that won't happen."

BB&T expects Arch to have a net debt-to-EBITDA ratio of 16.3x in 2015 that will grow to 17.0x in 2016.

258. On April 24, 2015, Arch also disclosed that, at its annual meeting, shareholders approved a reverse stock split of the outstanding and treasury shares of Company common stock a reverse stock split ratio of either 1-for-5 or 1-for-10, as determined by the Board. The Company had sought approval for a “Reverse Stock Split Proposal” in its proxy solicitation.

259. On May 5, 2015, Moody’s downgraded the corporate family rating (CFR) of Arch to Caa3 from Caa1 and the probability default rating (PDR) to Caa3-PD from Caa1-PD. The downgrade follows the continued stress on the coal sector, and the resulting deterioration in Arch’s credit metrics. Moody’s also downgraded the ratings on the senior secured term loan and bank revolving facility to Caa1 from B2, the second lien notes to Caa3 from Caa1, and all unsecured notes to Ca, from Caa2. Moody’s also affirmed the Speculative Grade Liquidity rating of SGL-3. The outlook is negative, and the ratings rationale reflected “the continued pressure on the company’s credit profile, and a capital structure that is deemed untenable in the current commodity price environment.” Moody’s further opined that “[t]he CFR reflects the extremely weak debt protection metrics and high leverage (over 17x as measured by the debt/EBITDA ratio for the twelve months ended December 31, 2014), which we do not expect to improve given weak metallurgical and thermal coal market conditions. We believe that metallurgical and thermal coal prices are unlikely to recover within the next eighteen months to a level that would contribute to a meaningful turnaround in performance. Consequently, we expect further strain on the company’s liquidity and debt protection measures.”

260. On May 21, 2015, Arch received a notice from the New York Stock Exchange that it did not satisfy the NYSE's continued listing standard requiring the average closing price of a listed company's common stock to be at least \$1.00 per share for any period of 30 consecutive trading days.

261. On May 22, 2015, *The Wall Street Journal* reported in an article entitled “Arch Coal Taps Restructuring Advisers Amid Debt; Deep coal-market slump continues to weigh on mining company” that

Arch Coal Inc. has tapped restructuring advisers to explore ways to decrease its multibillion-dollar debt load, according to people familiar with the matter, as a deep coal-market slump continues to weigh on the mining company and its rivals.

The St. Louis company is working with lawyers at Davis Polk & Wardwell LLP and financial advisers at Blackstone Group LP, the people said. Arch isn’t planning a broad restructuring of its debt load through bankruptcy, they added. Instead, it is looking to trim its debt through deals with bondholder groups.

Arch’s effort is the latest sign of how coal companies are contending with a long-term swoon in the industry, which is struggling as power plants switch to less-expensive natural gas and as demand falls for the type of coal used in steelmaking.

The weak market has forced Appalachian miners Patriot Coal Corp. and Xinerger Ltd. to file for chapter 11 bankruptcy protection this year. Another coal producer, Walter Energy Inc., earlier this month said it was discussing recapitalization options with creditors. Murray Energy Corp. is set to announce layoffs of about 21% of its workforce, due to weak pricing for the type of coal burned by power plants, *The Wall Street Journal* reported Thursday, and Alpha Natural Resources Inc. said Friday it is planning to lay off 439 workers .

Arch is in talks with holders of its bonds due in 2020, according to people familiar with the negotiations. One potential option is to swap the bonds for new, higher-ranking debt, the people said.

The bondholders, advised by investment bank Moelis & Co., include Blackstone’s credit arm, GSO Capital Partners; and hedge fund Hutchin Hill Capital LP, one of the people added. The bonds recently traded at around 32 cents on the dollar, according to MarketAxess.

Arch has \$5.1 billion in long-term debt, the legacy of its \$3.4 billion acquisition of International Coal Group Inc. in 2011 and a three-year streak of annual losses. As of March 31, it had about \$939 million in cash and short-term investments and \$179 million

in borrowing capacity under its lines of credit, according to a regulatory filing.

The company's shares fell 4% Friday to close at 66 cents.

262. On or about May 26, 2015, Credit Suisse analyst Nathan Littlewood said that of U.S. coal equities, "Alpha Natural Resources and Arch Coal have the most over-levered balance sheets and the highest recapitalization risk. Our bottoms-up, company level liquidity analysis indicates that Alpha Natural Resources shoulders the greatest liquidity risk, as negative FCF and upcoming debt maturities eat into its existing liquidity position. Arch Coal fairs somewhat better by our projections, though we still expect it to burn through cash for the next several quarters. Both companies are limited in their ability to borrow more debt and both face revolver maturities in mid-2016..." Littlewood noted that Arch has "one of the worst" balance sheets of coal companies. As a result, Littlewood initiated Arch Coal with an Underperform rating and 50 cent target price.

263. On May 27, 2015, Dow Jones Institutional News reported in an article entitled "Coal: Survival of the Fittest – Barron's Blog" that:

Yesterday, Credit Suisse warned that coal miners Arch Coal (ACI), Alpha Natural Resources (ANR) and Peabody Energy (BTU) were in "dire straits." Today, Citigroup's Ivan Szpakowski and team note that it will be "survival of the fittest" for the world's coal miners. They explain why:

Both thermal and metallurgical coal prices have fallen dramatically since 2011. While we believe that current prices are below sustainable long-run levels, we do not expect a return to prices anywhere near the levels seen a few years ago. We lower our long-run thermal coal price forecast to \$80/t from \$90/t (NEWC) and our met coal price forecast to \$125/t from \$170/t (HCC FOB Australia)...

Our new long-run price forecasts are primarily set off estimates for sustaining costs at currently operating mines given our expectation that weak demand and a small number of low-cost projects will render higher cost projects unnecessary. Our long-run price is thus

primarily sensitive to assumptions of cost inflation and longer-term demand...

Risks skewed to the downside -- China and India represent the largest sources of risk to our long-run forecasts. We believe such risks are skewed to the downside, particularly for met coal, where China could re-emerge as a net exporter. Indian domestic thermal coal production and potential PCI adoption are also key variables.

Shares of Arch Coal have fallen 1.3% to 57.2 cents at 10:14 a.m. today, while Peabody Energy has gained 2.4% to \$3.49, and Alpha Natural Resources has dropped 4.2% to 57.2 cents.

264. On May 27, 2015, *SNL Energy Finance Daily* reported in an article entitled “Tuesday’s Energy Stocks: Coal equities slip following analyst report” that:

Coal stocks headlined losses across energy sectors on Tuesday, May 26, with the SNL Coal Index falling 4.57% to 121.94.

Credit Suisse recently noted that U.S. coal equities can be snagged on the cheap, but that there is also a “dire macro outlook” leading to “increasingly troublesome balance sheets and liquidity issues.”

“While we see an options-based approach as being necessary for this sector, the value of an option is highly contingent upon time to expiration and ones’ view on commodity prices,” the report stated. “The shale revolution in the U.S. and oil sands in Canada have led to a structurally different energy-pricing regime in North America. ... When the rules to the game change, so can the outcomes.”

According to the report, Credit Suisse initiated coverage of Arch Coal Inc. and Alpha Natural Resources Inc. at “underperform,” Peabody Energy Corp. at “neutral” and Cloud Peak Energy Inc. at “outperform.”

Arch Coal, which received a delisting notice last week, sank 12.41% in heavy trading to close at 58 cents. Alpha Natural Resources lost 8.22% in strong trading to close at 60 cents, Peabody slid 6.06% in weak volume to finish at \$3.41 and Cloud Peak Energy fell 0.49% in above-average trading to close at \$6.13.

265. Since the beginning of the Relevant Period through the filing of the instant Complaint, the Plan's imprudent investments in Arch Stock have been decimated:



Source: www.google.com/finance?q=ACI

DEFENDANTS KNEW OR SHOULD HAVE KNOWN ARCH STOCK IMPRUDENT FOR THE PLAN, YET FAILED TO PROTECT PARTICIPANTS

266. During the Relevant Period, although they knew or should have known that Company Stock was an imprudent investment for the Plan, Defendants did nothing to protect the significant investment of Participants' retirement savings in Arch Stock.

267. As a result of the enormous erosion of the value of Arch Stock, the Participants, the retirement savings of whom were heavily invested in Arch Stock, suffered unnecessary and unacceptable losses.

268. Because of their high ranking positions within the Company and/or their status as fiduciaries of the Plan, Defendants knew or should have known of the existence of the above-mentioned problems.

269. Defendants knew or should have known that, due to the Company's exposure to losses stemming from the problems described above, Company Stock was imprudent no matter what its price. Regardless, the price of Company Stock inevitably dropped drastically and steadily beginning in 2011, the year before the start of the Relevant Period, and continued

throughout the Relevant Period due to the pervasive problems facing the Company. There was absolutely no objective evidence that the Company Stock price would or could recover. Yet, Defendants failed to protect the Plan and the Participants from these foreseeable losses.

270. As a result of Defendants' knowledge of and/or implication in creating and maintaining public and/or Participant misconceptions concerning Arch's true financial health, or at least its financial prospects, any generalized warnings of market and diversification risks that were made to the Participants regarding the Plan's investment in Arch Stock did not effectively inform the Participants of the dangers of investing in Company Stock.

271. In addition, upon information and belief, Defendants failed to adequately review the performance of the other fiduciaries of the Plan to ensure that they were fulfilling their fiduciary duties under the Plan and ERISA. Defendants also failed to conduct an appropriate investigation into whether Arch Stock was a prudent investment for the Plan and, in connection therewith, failed to provide the Participants with information regarding Arch's problems so that Participants—to the extent that they were permitted—could make informed decisions regarding whether to include Arch Stock in their accounts in the Plan.

272. An adequate (or even cursory) investigation by Defendants would have revealed to a reasonable fiduciary that investment by the Plan in Arch Stock during the Relevant Period was clearly imprudent. A prudent fiduciary acting under similar circumstances would have acted during the Relevant Period to protect the Participants against unnecessary losses, and would have made different investment decisions. Either Defendants did not conduct such an adequate investigation (in violation of their duty of prudence) or they did conduct an adequate investigation and ignored the results thereof (in violation of their duty of loyalty).

273. Because Defendants knew or should have known that Arch Stock was imprudent for the Plan during the Relevant Period, they had an obligation to protect the Plan and its Participants from unreasonable and entirely predictable losses incurred during the Relevant Period as a result of the Plan's investment in Arch Stock.

274. Defendants had available to them several different options for satisfying this duty, including, among other things: divesting the Plan of Arch Stock; discontinuing further contributions to and/or investment in Arch Stock under the Plan; resigning as fiduciaries of the Plan if, as a result of their employment by Arch, they could not loyally serve the Plan and its Participants in connection with the Plan's acquisition and holding of Arch Stock; making appropriate public disclosures as necessary; and/or consulting independent fiduciaries regarding appropriate measures to take in order to prudently and loyally serve the Participants of the Plan.

275. Despite the availability of these and other options, Defendants failed to take any adequate action during the Relevant Period to protect Participants from losses resulting from the Plan's investment in Arch Stock, instead standing idly by as the Plan's assets, along with tens of millions of dollars of Participants' retirement savings, were decimated.

CLAIMS FOR RELIEF UNDER ERISA

276. At all relevant times, Defendants are/were and acted as fiduciaries within the meaning of ERISA § 3(21)(A), 29 U.S.C. § 1002(21)(A).

277. ERISA § 502(a)(2), 29 U.S.C. § 1132(a)(2), provides, in pertinent part, that a civil action may be brought by a participant for relief under ERISA § 409, 29 U.S.C. § 1109.

278. ERISA § 409(a), 29 U.S.C. § 1109(a), "Liability for Breach of Fiduciary Duty," provides, in pertinent part, that any person who is a fiduciary with respect to a plan who breaches any of the responsibilities, obligations, or duties imposed upon fiduciaries by this title shall be personally liable to make good to such plan any losses to the plan resulting from each such

breach, and to restore to such plan any profits of such fiduciary which have been made through use of assets of the plan by the fiduciary, and shall be subject to such other equitable or remedial relief as the court may deem appropriate, including removal of such fiduciary.

279. ERISA § § 404(a)(1)(A) and (B), 29 U.S.C. § § 1104(a)(1)(A) and (B), provide, in pertinent part, that a fiduciary shall discharge his duties with respect to a plan solely in the interest of the participants, for the exclusive purpose of providing benefits to participants, and with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims.

280. These fiduciary duties under ERISA § § 404(a)(1)(A) and (B) are referred to as the duties of loyalty, exclusive purpose and prudence and, as courts have noted, “the duties of prudence and loyalty embodied in [ERISA § 404(a)(2)] have been characterized as the ‘highest known to law.’” *See, e.g., Shannahan v. Dynegy, Inc.*, No. 06-cv-0160, 2006 WL 3227319, at *4 (S.D. Tex. Nov. 6, 2006) (quoting *Sommers Drug Stores Co. Employee Profit Sharing Trust v. Corrigan*, 793 F.2d (5th Cir. 1986)).

281. These duties entail, among other things:

- a. the duty to conduct an independent and thorough investigation into, and continually to monitor, the merits of all the investment alternatives of a plan;
- b. the duty to avoid conflicts of interest and to resolve them promptly when they occur. A fiduciary must always administer a plan with an “eye single” to the participants’ interests, regardless of the interests of the fiduciaries themselves or the plan sponsor;
- c. the duty to disclose and inform, which encompasses: (1) a negative duty not to misinform; (2) an affirmative duty to inform when the fiduciary knows or should know

that silence might be harmful; and (3) a duty to convey complete and accurate information material to the circumstances of participants.

282. ERISA § 405(a), 29 U.S.C. § 1105 (a), “Liability for breach by co-fiduciary,” provides, in pertinent part, that:

[I]n addition to any liability which he may have under any other provision of this part, a fiduciary with respect to a plan shall be liable for a breach of fiduciary responsibility of another fiduciary with respect to the same plan in the following circumstances: (A) if he participates knowingly in, or knowingly undertakes to conceal, an act or omission of such other fiduciary, knowing such act or omission is a breach; (B) if, by his failure to comply with section 404(a)(1), 29 U.S.C. § 1104(a)(1), in the administration of his specific responsibilities which give rise to his status as a fiduciary, he has enabled such other fiduciary to commit a breach; or (C) if he has knowledge of a breach by such other fiduciary, unless he makes reasonable efforts under the circumstances to remedy the breach.

283. Plaintiff therefore brings this action under ERISA § 502(a) for Plan-wide relief under ERISA § 409(a) to recover losses sustained by the Plan arising out of the breaches of fiduciary duties by Defendants for violations under ERISA § 404(a)(1) and ERISA § 405(a).

COUNT I:

FAILURE TO PRUDENTLY AND LOYALLY MANAGE THE PLAN’S ASSETS (BREACHES OF FIDUCIARY DUTIES IN VIOLATION OF ERISA § § 404 AND 405 BY THE RETIREMENT COMMITTEE DEFENDANTS)

284. Plaintiff incorporates the allegations contained in the previous paragraphs of this Complaint as if fully set forth herein.

285. At all relevant times, as alleged above, the Retirement Committee Defendants were fiduciaries of the Plan within the meaning of ERISA § 3(21)(A), 29 U.S.C. § 1002(21)(A), in that they exercised discretionary authority or control over the administration and/or management of the Plan and/or disposition of the Plan’s assets.

286. Under ERISA, fiduciaries who exercise discretionary authority or control over management of a plan or disposition of a plan's assets are responsible for ensuring that all investment options made available to participants under a plan are prudent. Furthermore, such fiduciaries are responsible for ensuring that assets within the plan are prudently invested. The Retirement Committee Defendants were responsible for ensuring that all investments in the Company's stock in the Plan were prudent. The Retirement Committee Defendants are liable for losses incurred as a result of such investments being imprudent.

287. A fiduciary's duty of loyalty and prudence requires it to disregard plan documents or directives that it knows or reasonably should know would lead to an imprudent result or would otherwise harm plan participants. ERISA § 404(a)(1)(D), 29 U.S.C. § 1104(a)(1)(D). Thus, a fiduciary may not blindly follow plan documents or directives that would lead to an imprudent result or that would harm plan participants, nor may it allow others, including those whom they direct, or who are directed by the plan, including plan trustees, to do so.

288. The Retirement Committee Defendants' duty of loyalty and prudence also obligated them to speak truthfully to Participants, not to mislead them regarding the Plan or its assets, and to disclose information that Participants needed in order to exercise their rights and interests under the Plan. This duty to inform Participants includes an obligation to provide Participants with complete and accurate information, and to refrain from providing inaccurate or misleading information, or concealing material information, regarding Plan investments/investment options such that Participants can make informed decisions with regard to the prudence of investing in such options made available under the Plan.

289. The Retirement Committee Defendants breached their duties to prudently and loyally manage the Plan's assets. During the Relevant Period, the Retirement Committee

Defendants knew or should have known that, as described herein, Company Stock was not a suitable and appropriate investment for the Plan. Yet, during the Relevant Period, despite their knowledge of the imprudence of the investment, the Retirement Committee Defendants failed to take any meaningful steps to protect Participants from the inevitable losses that they knew would ensue as the already-weakened Arch faced quarter after quarter of loss as its business model became increasingly difficult and its ultimate demise became more likely.

290. The Retirement Committee Defendants further breached their duties of loyalty and prudence by failing to divest the Plan of Company Stock during the Relevant Period when they knew or should have known that it was not a suitable and appropriate investment for the Plan.

291. The Retirement Committee Defendants also breached their duties of loyalty and prudence by failing to provide complete and accurate information regarding the Company's true financial condition and, generally, by conveying inaccurate information regarding the Company's future outlook. During the Relevant Period, upon information and belief, the Company fostered a positive attitude toward Company Stock, and/or allowed Participants in the Plan to follow their natural bias towards investment in the equities of their employer by not disclosing negative material information concerning the imprudence of investment in Company Stock. As such, Participants could not appreciate the true risks presented by investments in Arch Stock and therefore could not make informed decisions regarding their investments in the Plan.

292. The Retirement Committee Defendants also breached their co-fiduciary obligations by, among their other failures, knowingly participating in each other's failure to protect the Plan from inevitable losses. The Retirement Committee Defendants had or should

have had knowledge of such breaches by other fiduciaries of the Plan, yet made no effort to remedy them.

293. As a direct and proximate result of the breaches of fiduciary duties during the Relevant Period alleged herein, the Plan and, indirectly, the Participants lost a significant portion of their retirement investments. Had the Retirement Committee Defendants taken appropriate steps to comply with their fiduciary obligations during the Relevant Period, Participants could have liquidated some or all of their holdings in Company Stock and thereby eliminated, or at least reduced, losses to the Plan and themselves.

294. Pursuant to ERISA § 502(a), 29 U.S.C. § 1132(a) and ERISA § 409, 29 U.S.C. § 1109(a), Defendants in this Count are liable to restore the losses (including lost profits) to the Plan caused by their breaches of fiduciary duties alleged in this Count.

COUNT II:

FAILURE TO ADEQUATELY MONITOR OTHER FIDUCIARIES AND PROVIDE THEM WITH ACCURATE INFORMATION (BREACHES OF FIDUCIARY DUTIES IN VIOLATION OF ERISA § 404 BY THE MONITORING DEFENDANTS)

295. Plaintiff incorporates the allegations contained in the previous paragraphs of this Complaint as if fully set forth herein.

296. At all relevant times, as alleged above, the Monitoring Defendants were fiduciaries of the Plan, within the meaning of ERISA § 3(21)(A), 29 U.S.C. § 1002(21)(A). Thus, they were bound by the duties of loyalty, exclusive purpose, and prudence.

297. As alleged above, the scope of the fiduciary responsibilities of the Monitoring Defendants included the responsibility to appoint, remove, and, thus, monitor the performance of other Plan fiduciaries.

298. Under ERISA, a monitoring fiduciary must ensure that monitored fiduciaries are performing their fiduciary obligations, including those with respect to the investment and holding of a plan's assets, and must take prompt and effective action to protect the plan and participants when they are not.

299. The monitoring duty further requires that appointing fiduciaries have procedures in place so that on an ongoing basis they may review and evaluate whether the "hands-on" fiduciaries are doing an adequate job (for example, by requiring periodic reports on their work and the plan's performance, and by ensuring that they have a prudent process for obtaining the information and resources they need). In the absence of a sensible process for monitoring their appointees, the appointing fiduciaries would have no basis for prudently concluding that their appointees were faithfully and effectively performing their obligations to the plan's participants or for deciding whether to retain or remove them.

300. Furthermore, a monitoring fiduciary must provide the monitored fiduciaries with complete and accurate information in their possession that they know or reasonably should know that the monitored fiduciaries must have in order to prudently manage the plan and the plan's assets, or that may have an extreme impact on the plan and the fiduciaries' investment decisions regarding the plan.

301. During the Relevant Period, the Monitoring Defendants breached their fiduciary monitoring duties by, among other things:

a. failing, at least with respect to the Plan's investment in Company Stock, to properly monitor their appointee(s), to properly evaluate their performance, or to have any proper system in place for doing so, and standing idly by as the Plan suffered enormous losses as a result of the appointees' imprudent actions and inaction with respect to Company Stock;

b. failing to ensure that the monitored fiduciaries appreciated the true extent of the Company's precarious financial situation and the likely impact that financial failure would have on the value of the Plan's investment in Company Stock;

c. to the extent any appointee lacked such information, failing to provide complete and accurate information to all of their appointees such that they could make sufficiently informed fiduciary decisions with respect to the Plan's assets and, in particular, the Plan's investment in Company Stock; and

d. failing to remove appointees whose performance was inadequate in that they continued to permit the Plan to make and maintain investments in the Company Stock despite the practices that rendered it an imprudent investment during the Relevant Period.

302. As a consequence of the Monitoring Defendants' breaches of fiduciary duty, the Plan suffered tremendous losses. If the Monitoring Defendants had discharged their fiduciary monitoring duties as described above, the losses suffered by the Plan would have been minimized or avoided.

303. The Monitoring Defendants are liable as co-fiduciaries because they knowingly participated in each other's fiduciary breaches as well as those by the monitored fiduciaries, they enabled the breaches by those Defendants, and they failed to make any effort to remedy these breaches despite having knowledge of them.

304. Therefore, as a direct and proximate result of the breaches of fiduciary duty by the Monitoring Defendants during the Relevant Period alleged herein, the Plan and, indirectly, the Participants, lost tens of millions of dollars of retirement savings.

305. Pursuant to ERISA § § 409, 502(a)(2) and (a)(3), 29 U.S.C. § § 1109, 1132(a)(2) and (a)(3), the Monitoring Defendants are liable to restore the losses to the Plan caused by their

breaches of fiduciary duties alleged in this Count and to provide other equitable relief as appropriate.

COUNT III:

**FAILURE TO PRUDENTLY AND LOYALLY MANAGE THE PLAN'S ASSETS
(BREACHES OF FIDUCIARY DUTIES IN VIOLATION OF ERISA § § 404 AND 405 BY
MERCER)**

306. Plaintiff incorporates the allegations contained in the previous paragraphs of this Complaint as if fully set forth herein.

307. At all relevant times, as alleged above, Defendant Mercer was a fiduciary of the Plan within the meaning of ERISA § 3(21)(A), 29 U.S.C. § 1002(21)(A) in that it exercised discretionary authority or control over the administration and/or management of the Plan or disposition of the Plan's assets.

308. Under ERISA, fiduciaries who exercise discretionary authority or control over management of a plan or disposition of a plan's assets are responsible for ensuring that all investment options made available to participants under a plan are prudent. Furthermore, such fiduciaries are responsible for ensuring that assets within the plan are prudently invested. Mercer could not blindly follow directions of the Retirement Committee Defendants if it knew or should have known such directions were improper under ERISA.

309. A directed trustee's duty of prudence requires it to disregard plan documents or directives that it knows or reasonably should know would lead to an imprudent result or would otherwise harm plan participants. ERISA § 404(a)(1)(D), 29 U.S.C. § 1104(a)(1)(D). Thus, a fiduciary may not blindly follow plan documents or directives that would lead to an imprudent result or that would harm plan participants, nor may it allow others, including those whom they direct, or who are directed by the plan, including plan trustees, to do so.

310. Mercer breached its duties to prudently and loyally manage the Plan's assets. During the Relevant Period, Mercer knew or should have known that, as described herein, Company Stock was not a suitable and appropriate investment for the Plan. Yet, during the Relevant Period, despite its knowledge of the imprudence of the investment, Mercer failed to take any meaningful steps to protect Participants from the inevitable losses that it knew would ensue as the already-weakened Arch faced quarter after quarter of loss as its business model became increasingly difficult and its ultimate demise became significantly more likely.

311. Mercer further breached its duties of loyalty and prudence by failing to divest the Plan of Company Stock when it knew or should have known that it was not a suitable and appropriate investment for the Plan.

312. Mercer also breached its co-fiduciary obligations by, among their other failures, knowingly participating in each other's failure to protect the Plan from inevitable losses. Mercer had or should have had knowledge of such breaches by other fiduciaries of the Plan, yet made no effort to remedy them.

313. As a direct and proximate result of the breaches of fiduciary duties alleged herein, the Plan, and indirectly the Participants, lost a significant portion of their retirement investment. Had Mercer taken appropriate steps to comply with its fiduciary obligations, participants could have liquidated some or all of their holdings in Company Stock and thereby eliminated, or at least reduced, losses to the Plan.

314. Pursuant to ERISA § 502(a), 29 U.S.C. § 1132(a) and ERISA § 409, 29 U.S.C. § 1109(a), Defendant in this Count is liable to restore the losses to the Plan caused by its breaches of fiduciary duties alleged in this Count.

CAUSATION

315. The total Arch Stock price collapse of over 96%, which devastated the Plan's assets, and could have and would have been avoided in whole or in part by Defendants complying with their ERISA fiduciary duties. Defendants could have taken certain actions based on the publicly known information alone such as, and not limited to: investigating whether Arch was a prudent retirement investment; retaining outside advisors to consult them or to act as fiduciaries; seeking guidance from governmental agencies (such as the DOL or SEC); resigning as fiduciaries of the Plan; stopping or limiting additional purchases of Arch Stock by the Plan; and/or by divesting the Arch Stock held by the Plan.

316. Despite these and other options, Defendants—who knew or should have known that Arch was an imprudent retirement investment—chose to, as fiduciaries, continue allowing the Plan to acquire further Arch Stock, while taking no action to protect their wards as Arch's condition worsened and the Plan Participants' retirement savings were decimated. Prudent fiduciaries would have acted otherwise and taken appropriate actions to protect the Plan and its Participants.

317. To the extent Defendants wanted to take action based on non-publicly disclosed information that they were privy to, the following alternative options—which are pled as alternative statements under FED. R. CIV. P. 8(d)(2) to the extent they are inconsistent—were available to Defendants and (a) could have been done without violating securities laws or any other laws, (b) should have been done to fulfill Defendants' fiduciary obligations under ERISA, and (c) would not have been more likely to harm the Plan than to help it.

318. First, Defendants could have and should have directed that all Company and Participant contributions to the Company Stock fund be held in cash rather than be used to purchase Arch Stock. The refusal to purchase Company Stock for the Company Stock fund is

not a “transaction” within the meaning of insider trading prohibitions. This action would not have required any independent disclosures that could have had a materially adverse effect on Arch’s stock price.

319. Alternatively, Defendants should have closed the Fund itself to further contributions and directed that contributions be diverted from the Fund into other (prudent) investment options based upon Participants’ instructions or, if there were no such instructions, the Plan’s default investment option.

320. Additionally, because Defendants could and should have concluded that Arch stock was an imprudent retirement savings vehicle based solely upon public information, no disclosure was required before conducting an orderly liquidation of the Plan’s holdings.

321. Defendants also could have:

- sought guidance from the DOL or SEC as to what they should have done;
- resigned as Plan fiduciaries to the extent they could not act loyally and prudently; and/or
- retained outside experts to serve either as advisors or as independent fiduciaries specifically for the Plan and not the Company in general.

322. The Plan suffered tens of millions of dollars in losses during the Relevant Period because substantial assets of the Plan were imprudently invested, or allowed to be invested, by Defendants in Company Stock during the Relevant Period, in breach of Defendants’ fiduciary duties, as reflected in the diminished account balances of the Participants.

323. Had Defendants properly discharged their fiduciary and/or co-fiduciary duties, the Plan and the Participants would have avoided a substantial portion of the losses that they suffered through the Plan’s continued investment in Company Stock.

324. Given the totality of circumstances prevailing during the Relevant Period no prudent fiduciary would have made the same decision to retain the clearly imprudent Arch Stock as an investment in the Plan.

325. Despite the availability of these and other options, Defendants took no meaningful action during the Relevant Period to protect Participants from losses as a result of the Company Stock's imprudence until it was too late to make any substantial difference.

REMEDIES FOR BREACHES OF FIDUCIARY DUTY

326. As noted above, as a consequence of Defendants' breaches, the Plan suffered significant losses.

327. ERISA § 502(a), 29 U.S.C. § 1132(a) authorizes a plan participant to bring a civil action for appropriate relief under ERISA § 409, 29 U.S.C. § 1109. Section 409 requires "any person who is a fiduciary . . . who breaches any of the . . . duties imposed upon fiduciaries . . . to make good to such plan any losses to the plan...." Section 409 also authorizes "such other equitable or remedial relief as the court may deem appropriate...."

328. With respect to calculation of the losses to a plan, breaches of fiduciary duty result in a presumption that, but for the breaches of fiduciary duty, the Participants in the Plan would not have made or maintained its investments in the challenged investment and, where alternative investments were available, that the investments made or maintained in the challenged investment would have instead been made in the most profitable alternative investment available. In this way, the remedy restores the values of the Plan's assets to what they would have been if the Plan had been properly administered.

329. Plaintiff, the Plan, and the Participants are therefore entitled to relief from Defendants in the form of: (1) a monetary payment to the Plan to make good to the Plan the losses to the Plan resulting from the breaches of fiduciary duties alleged above in an amount to

be proven at trial based on the principles described above, as provided by ERISA § 409(a), 29 U.S.C. § 1109(a); (2) injunctive and other appropriate equitable relief to remedy the breaches alleged above, as provided by ERISA § § 409(a) and 502(a), 29 U.S.C. § § 1109(a) and 1132(a); (3) reasonable attorney fees and expenses, as provided by ERISA § 502(g), 29 U.S.C. § 1132(g), the common fund doctrine, and other applicable law; (4) taxable costs; (5) interests on these amounts, as provided by law; and (6) such other legal or equitable relief as may be just and proper.

330. Each Defendant is jointly and severally liable for the acts of the other Defendants as a co-fiduciary.

JURY DEMAND

Plaintiff demands a jury.

PRAYER FOR RELIEF

WHEREFORE, Plaintiff requests the following relief:

A. A Judgment that the Defendants, and each of them, breached their ERISA fiduciary duties to the Plan and the Participants during the Relevant Period;

B. A Judgment compelling the Defendants to make good to the Plan all losses to the Plan resulting from Defendants' breaches of their fiduciary duties, including losses to the Plan resulting from imprudent investment of the Plan's assets, and to restore to the Plan all profits the Defendants made through use of the Plan's assets, and to restore to the Plan all profits which the Plan would have made if the Defendants had fulfilled their fiduciary obligations;

C. A Judgment imposing a Constructive Trust on any amounts by which any Defendant was unjustly enriched at the expense of the Plan as the result of breaches of fiduciary duty;

D. A Judgment awarding actual damages in the amount of any losses the Plan suffered, to be allocated among the Participants' individual accounts in proportion to the accounts' losses;

E. A Judgment requiring that Defendants allocate the Plan's recoveries to the accounts of all participants who had any portion of their account balances invested in the common stock of Arch maintained by the Plan in proportion to the accounts' losses attributable to the decline in Arch's stock price;

F. A Judgment awarding costs pursuant to 29 U.S.C. § 1132(g);

G. A Judgment awarding attorneys' fees pursuant to 29 U.S.C. § 1132(g) and the common fund doctrine; and

H. A Judgment awarding equitable restitution and other appropriate equitable monetary relief against the Defendants.

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